SUPREME COURT, U. S.
FILED
FEB 5 1974

IN THE

Supreme Court of the United States

OCTOBER TERM, 1973.

No. 73 1201

CHICAGO AND NORTH WESTERN TRANSPORTATION COMPANY, GRAND TRUNK WESTERN RAILROAD COMPANY AND ST. LOUIS-SAN FRANCISCO RAILWAY COMPANY,

Petitioners,

vs.

GEORGE P. BAKER, RICHARD C. BOND, AND JERVIS LANGDON, JR., TRUSTEES OF THE PROPERTY OF PENN CENTRAL TRANSPORTATION COMPANY, DEBTOR,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

RICHARD M. FREEMAN,
ZEV STEIGER,
400 West Madison Street,
Chicago, Illinois 60606,
Attorneys for Petitioners.

Gunthorp-Warren Printing Company, Chicago • 346-1717

INDEX

PAGE

Opinions Below 2

Jurisdiction 2

Questions Presented 2

Statutory Provisions Involved 3

Statement of the Case 3

1. The Early Stages of This Proceeding 3
2. Nature of "Basic" Per Diem 4
3. Rules for Per Diem Settlement 5
4. Trustees' Petition and Opinion of the Reorganization Court 8
5. Opinion of the Court of Appeals 10

Reasons for Granting the Writ of Certiorari 11

1. The Decision of the Court of Appeals Is in Conflict with a Decision of the Supreme Court 11
2. A Determination by the Supreme Court of the Status of Pre-Reorganization Railroad Per Diem Claims and Whether Setoff or Other Relief Should Be Permitted, Is Necessary to the Proper Administration of Section 77 of the Bankruptcy Act in Conformity with Congressional Transportation Policy Embodied in the Interstate Commerce Act, Particularly Section 1(14)(a), and in the Last Sentence of Section 77(j) of the Bankruptcy Act 13

Conclusion 16

Appendix:

District Court Opinion and Order No. 613 Filed March 16, 1972 ..... A1
Court of Appeals Opinion Filed October 9, 1973... A16
Court of Appeals Order Amending Opinion Filed November 6, 1973 ..... A43
Court of Appeals Amended Judgment on Reargument Filed November 6, 1973 ..... A45
Court of Appeals Order Denying Petitions for Rehearing Filed November 7, 1973 ..... A48
Statutory Provisions Involved A50
Interstate Commerce Act A50
49 U. S. C. § 1(4) A50
49 U. S. C. § 1(10) A50
49 U. S. C. § 1(11) A50
49 U. S. C. § 1(14)(a) A51
49 U. S. C. § 15(8) A52
Bankruptcy Act A52
11 U.S.C. § 205(j) A52
Interstate Commerce Commission Orders A54
I.C.C. Order, dated July 15, 1930 (Rules for Car-Hire Settlement, Docket No. 17801) ... A54
I.C.C. Order, dated May 28, 1970 (Chicago, Burlington & Quincy R.R. Co., et al v. New York, Susquehanna & Western R.R. Co., et al., Docket No. 31358) A57

TABLE OF CITATIONS

Cases

Baltimore & O. R. Co. v. New York, N. H. & H. R. Co., 196 F. Supp. 724 (S.D. N. Y. 1961) 8

Boston and Maine Railroad v. United States, 297 F. Supp. 615 (D. Mass. 1969) aff'd per curiam, 396 U. S. 27 (1969) 4

Chicago, R. I. & P. Ry. Co. v. U. S., 284 U. S. 80 (1931) 4, 6, 8, 11, 12

In re Central Railroad of New Jersey, 273 F. Supp. 282 (D. N. J. 1967), aff'd. per curiam, 392 F. 2d 589 (3d Cir. 1968) 10

Southern Ry. Co. v. Flournoy, 301 F. 2d 847 (4th Cir. 1962) 9-10, 12

Union Pacific Railroad Company v. United States, 300 F. Supp. 318 (D. Neb. 1969) aff'd. per curiam, 396 U. S. 27 (1969) 4

United States v. Allegheny-Ludlum Steel Corp., 406 U. S. 742 (1972) 4

I. C. C. Proceedings.

Chicago, B. & Q. R. Co. v. New York, S. & Western R. Co., 332 I. C. C. 176 (1968) 4, 5, 6, 7, 14

Rules for Car Hire Settlement, 160 I. C. C. 369, 165 1. C. C. 495 (1930) 6, 7, 8, 10, 11

Statutes.

Bankruptcy Act, Section 77, 11 U. S. C. § 205 . . . 2, 13, 14, 15

28 U. S. C. § 1254(1) 2

Interstate Commerce Act:

49 U. S. C. § 1254(1) 2

49 U. S. C. § 1(4) 4

49 U. S. C. § 1(10) 4

49 U. S. C. § 1(11) 4, 6

49 U. S. C. § 1(14)(a) 4, 5, 6, 13, 14, 15

49 U. S. C. § 15(8) 4, 8

Interstate Commerce Commission Orders.

I. C. C. Order, dated July 15, 1930 (Rules for Car-Hire Settlement, Docket No. 17801) 6, 10, 12

I. C. C. Order, dated May 28, 1970 (Chicago, Burlington & Quincy R. R. Co., et al. v. New York, Susquehana & Western R. R. Co., et al., Docket No. 31358) 5, 6, 7

Rules Governing Interline Accounts

Code of Per Diem Rules Circular No. OT-10-B (effective Jan. 1, 1968), published by Operating-Transporation Division, AAR 5, 6, 7, 12

Disbursement Mandatory Rules on *Railway Accounting Rules* published by the Accounting Division, Association of American Railroads (effective Oct. 1, 1969) and its Supplement (effective Sept. 1, 1970) 7

IN THE

Supreme Court of the United States

OCTOBER TERM, 1973.

No.

CHICAGO AND NORTH WESTERN TRANSPORTATION COMPANY, GRAND TRUNK WESTERN RAILROAD COMPANY AND ST. LOUIS-SAN FRANCISCO RAILWAY COMPANY,

Petitioners,

vs.

GEORGE P. BAKER, RICHARD C. BOND, AND JERVIS LANGDON, JR., TRUSTEES OF THE PROPERTY OF PENN CENTRAL TRANSPORTATION COMPANY, DEBTOR,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

Petitioners, Chicago and North Western Transportation Company ("North Western"), Grand Trunk Western Railroad Company ("Grand Trunk") and St. Louis-San Francisco Railway Company ("Frisco"), petition for a Writ of Certiorari to review the judgment (on reargument) of the United States Court of Appeals for the Third Circuit, sitting *en banc*, entered on October 9, 1973, as amended by its judgment entered on November 6, 1973 (rehearing denied November 7, 1973), to the extent that it affirmed in part Order No. 613 of the United States

District Court for the Eastern District of Pennsylvania entered on March 16, 1972, in the Debtor's reorganization proceedings pursuant to Section 77 of the Bankruptcy Act (11 U. S. C. § 205).

OPINIONS BELOW.

The opinion of the United States District Court for the Eastern District of Pennsylvania is reported at 340 F. Supp. 857 (E. D. Pa. 1972) and is printed in the Appendix (A1). The opinion of the Court of Appeals for the Third Circuit, filed October 9, 1973, as amended by its order filed November 6, 1973, is not reported. The opinion and amending order are printed in the Appendix (A16, A43).

JURISDICTION.

The judgment on reargument of the United States Court of Appeals for the Third Circuit was entered October 9, 1973, and an amended judgment was entered on November 6, 1973. Petitions for rehearing were denied by order dated November 7, 1973 (A48).

This Court's jurisdiction is invoked pursuant to 28 U. S. C. § 1254(1).

QUESTIONS PRESENTED.

1. Whether, in a Section 77 reorganization, the pre-reorganization per diem balances which arise from freight car interchange made mandatory by the Interstate Commerce Act, and which by order of the Interstate Commerce Commission must be settled in accordance with prescribed rules, are claims of involuntary creditors superior to claims of voluntary creditors.

2. Whether a reorganization court must order payment or permit setoff of pre-organization railroad per diem claims, or declare an equitable lien or constructive trust for such claims.

STATUTORY PROVISIONS INVOLVED.

Sections 1(4), 1(10), 1(11), 1(14)(a) and 15(8) of the Interstate Commerce Act (49 U. S. C. § 1 et seq.) and Section 77(j) of the Bankruptcy Act (11 U. S. C. 205(j)) are set forth in the Appendix hereto A50-A53.

STATEMENT OF THE CASE.

1. The Early Stages of This Proceeding.

On June 21, 1970, Penn Central Transportation Company ("Penn Central") filed a petition for reorganization under Section 77 of the Bankruptcy Act. The Reorganization Court, in approving the petition that day, authorized Penn Central, in its discretion, to pay all interline balances owed by it to other railroads on interline accounts (A5-A6). These accounts—Freight, Passenger, Per Diem, Switching, Loss and Damage, Overcharge and Car Repairs—are summarized in the opinion of the Reorganization Court (A3-A5),[1] and are the accounts by which the nation's railroads settle among themselves interline transactions required by joint service over connecting lines.

When Penn Central declined to pay any interline balances after June 21, 1970, the Reorganization Court, upon the railroads' motion to compel payment, entered Order No. 9 making mandatory the payment by Penn Central of post-reorganization interline balances stated from and after July 1, 1970 (Jt. App. 32a-33a; A6). The Court expressly left open the question of the status of pre-reorganization interline balances not required to be paid by Order No. 9 (A7).

Substantial pre-reorganization interline balances were owed by Penn Central to Petitioners and other railroads (Jt. App. 38a), and by the railroads to Penn Central (Jt. App. 34a).

1. The reference "A . . ." is to the Appendix to this petition; the reference "Jt. App. . . a" is to the Joint Appendix filed in the Court of Appeals.

Among these were undisputed balances (A1-A2) in the Per Diem Account of $700,000, $240,000 and $180,000 owed by Penn Central to Petitioners, North Western, Grand Trunk and Frisco, respectively, for Penn Central's use of their freight cars in April 1970 and prior months.

2. Nature of "Basic" Per Diem.

By participating in interline transportation of freight over through routes, a railroad daily moves loaded and empty cars owned by other railroads. Some means is therefore required to equitably apportion among the railroads the burden of acquiring and maintaining what is in essence "a single common pool"[2] used by all. Because the Interstate Commerce Act makes use of foreign cars compulsory on both owner and user,[3] the compensation to which the owner is entitled under the Act[4] may not be more than the average cost the user would have incurred as owner of the car or by use of its own car.[5] Thus the charge to the user is no more than a sharing of cost, and includes no element of profit to the owner;[6] it is not ordinary rent, and the relationship of the parties is not that of lessor and lessee.[7]

Petitioners' per diem balances against Penn Central represent the amount by which the compensation Penn Central was required to pay to them for use of their cars in April 1970 (and prior months) exceeded the compensation they were required to

2. *United States* v. *Allegheny-Ludlum Steel Corp.*, 406 U. S. 742, 743 (1972).

3. 49 U. S. C. § 1(4), § 15(8); *Chicago, R. I. & P. Ry. Co.* v. *U. S.*, 284 U. S. 80, 91, 101-102 (1931).

4. 49 U. S. C. § 1(14)(a); also, 49 U. S. C. § 1(10), § 1(11).

5. *Chicago, B. & Q. R. Co.* v. *New York, S. & Western R. Co.*, 332 I. C. C. 176, 186-88 (1968), *Boston and Maine Railroad* v. *United States*, 297 F. Supp. 615 (D. Mass. 1969), *Union Pacific Railroad Company* v. *United States*, 300 F. Supp. 318, 322-324, 330 (D. Neb. 1969), aff'd *per curiam*, 396 U. S. 27 (1969) (the *Time-Mileage* case).

6. *Id.*, p. 186.

7. *Id.*, p. 188.

pay Penn Central for use of its cars in the same period. The level of compensation (from August 1, 1969) was tentatively prescribed as a *per diem* rate (per car, per day) in Rule 1 of the Code of Per Diem Rules promulgated by the Association of American Railroads ("AAR") (Jt. App. 76a-77a), but following the *Time-Mileage* case,[8] the compensation was finally fixed by order of the Interstate Commerce Commission, served before but effective after June 21, 1970, when Penn Central's petition for reorganization was filed and approved.[9] In the *Time-Mileage* case the Commission found (at page 259) that under 49 U. S. C. § 1(14)(a), "reasonable compensation to car owners requires the payment by all railroads of the *time and mileage* rates set forth in Table C" of the report (emphasis added). This compensation is so-called "basic" per diem, which is predicated on average cost.[10]

3. Rules for Per Diem Settlement.

Petitioners were not only compelled by the Interstate Commerce Act to permit Penn Central to use their cars, they were also compelled by the Act to establish and enforce "just and

8. See footnote 5, *supra.*

9. In the *Time-Mileage* case (332 I. C. C. 176) the Interstate Commerce Commission, pursuant to its authority under § 1(14)(a) of the Interstate Commerce Act (49 U. S. C. § 1(14)(a)), found that uniform per diem rates for all railroads were required (*Id.*, p. 258), and ordered the railroads, including Penn Central, to pay after October 1, 1968, the car hire rates per day and per mile set forth in Table C of the report (*Id.*, p. 259); and by order served January 30, 1970, before the Reorganization Court on June 21, 1970, approved Penn Central's petition for reorganization, the Commission ordered that railroad per diem balances be adjusted and paid from August 1, 1969, on the basis of the proscribed time-mileage rates. That order became effective on September 1, 1970, after several Commission-ordered postponements (A57-A58). The Penn Central Trustees, apparently pursuant to Order No. 9 of the Reorganization Court, paid the time-mileage adjustment amounts in excess of the per diem balances owed by Penn Central to Petitioners, but the Trustees decline to pay such balances.

10. *Id.*, p. 186.

reasonable" per diem rules and practices,[11] and they were compelled to observe them by the July 15, 1930 order of the Interstate Commerce Commission in the *Per Diem Rules* case,[12] which required that all railroads 100 miles or more in length "shall make car-hire *settlements* direct with car owners in accordance with the per diem rules" (A54-A56, paragraph (4) (emphasis added)).

This order made mandatory the accounting and settlement practices Petitioners followed in June 1970 to obtain from Penn Central payment of their per diem balances. These practices were prescribed by the AAR Code of Per Diem Rules[13]

11. The Interstate Commerce Act imposes a duty upon each railroad "to establish, observe and enforce just and reasonable rules, regulations and practices with respect to car service" and expressly prohibits and declares unlawful every such unreasonable rule, regulation and practice (49 U. S. C. § 1(11)). Under 49 U. S. C. § 1(14)(a), the Interstate Commerce Commission is authorized to establish such reasonable rules and practices and punish for nonobservance. The rules "with respect to car service" include not only rules on compensation for use of foreign cars, but also "reasonable rules prescribing forms and methods of accounting, reporting and distributing payments in respect of such service." *Chicago, R. I. & P. Ry. Co.* v. *U. S., supra*, p. 95 (the *Rock Island* case).

12. *Rules for Car Hire Settlement*, 160 I. C. C. 369, 165 I. C. C. 495 (1930) (the *Per Diem Rules* case).

13. Under Rule 2 of the Code of Per Diem Rules, car days for which per diem accrued are reckoned (midnight to midnight) by subtracting the date of receipt (not paid for) from the date of delivery (paid for), with cars received and delivered the same day being "free" to the user. Rule 2 also provides that records of receipt and delivery be obtained from reports required by Rule 9. Under Rule 9, Interchange Reports (closing at midnight) must be made each day on all cars delivered that day and signed for both receiving and delivering roads, and Rule 10 requires the delivering road to promptly transmit to the car owner a Junction Report stating car data, time and place of interchange, and the names of the roads involved. Under Rule 11 the user must furnish the owner, *not later than the tenth day of the second month following the month in which the per diem accrued*, a per diem report showing the total per diem accrued to the owner's account in the reported month, and car data (including car mileage on the user's lines for months commencing August 1, 1969, as required by the orders in the *Time-Mileage* case); and Rule 12 prescribes that "*settlement* of amounts accruing for the use of cars shall be made *monthly*" (emphasis added).

(Jt. App. 76a-77a), established by agreement of the railroads, and were substantially identical to the practices in effect under the AAR Code of Per Diem Rules in 1930,[14] which the Commission, in the *Per Diem Rules* case (at page 397), found to be "apparently the best system yet devised"[15] for railroads which connect with a large number of other carriers.

The Commission's order was sustained by this Court in the *Rock Island* case,[16] and is still in effect. Thus, since the settlement rules and practices under the Code of Per Diem Rules were substantially identical in 1930 and 1970, Petitioners were compelled by the Interstate Commerce Act and by the Commission's order to settle their per diem balances with Penn Central exactly as they attempted to do.

For per diem accruing on the owner's car in any month, the settlement practice prescribed by the Commission's 1930 order compels the owner to wait at least until the tenth day of the second month following the month of per diem accrual, before it can demand payment from the user (Rules 11 and 12). This is true—even without that order—because the owner, to learn the amount owed it by each user, must rely upon the user to report the total per diem accrued on the user's lines (car days and car mileage included). Only then is it possible for the owner to demand payment, and the practice of settlement is completed by application of Disbursement Mandatory Rules 5 and 7 of the AAR Railway Accounting Rules (Jt. App. 134a). These rules repeat the reporting requirements under Rule 11 of the Code of Per Diem Rules, and specify that per

14. See *Rules for Car Hire Settlement, supra,* pp. 378-379, 395-397.

15. *Id.,* p. 397.

16. *Chicago, R. I. & P. Ry. Co.* v. *U. S., supra.* In reversing the decree of dismissal (without opinion) of the three-judge district court below, this Court upheld paragraphs (2) and (3) of the Commission's order, but held that paragraph (5), which is not material here, should have been set aside. Paragraphs (1) and (4) were not contested.

diem balances are to be settled on a net balance basis, with the net balance subject to draft immediately following exchange of per diem reports (Jt. App. 76a-77a). Settlement by draft on a net balance basis was also the practice followed by the railroads in 1930.[17]

Petitioners followed this car accounting and settlement practice in June 1970, as they were required to do by the Commission's 1930 order. Drafts were drawn following exchange of per diem reports and were presented for payment after June 21, 1970. Penn Central declined to honor the drafts, having entered reorganization. Yet there was no voluntary extension of credit to Penn Central. Even without the Commission order, Petitioners had no lawful means by which to protect themselves against non-payment of their per diem balances. They could not withhold their cars,[18] and since any demand by them for cash settlement or security would be disregarded by Penn Central with impunity, there was nothing more they could have done (or could do now) to protect themselves against non-payment.[19]

4. Trustees' Petition and Opinion of the Reorganization Court.

On June 24, 1971, the Trustees petitioned the Reorganization Court for an order directing Petitioners and other railroads to pay $4,300,000 in interline balances owing to Penn Central (Jt. App. 34a-35a). Petitioners, as members of the Committee of Interline Railroads, responded to the Trustees' petition through the Answer and Counterclaims of the Committee (Jt. App. 37a-47a). Petitioners alleged that each Petitioner is owed amounts which equal or exceed the amounts owed by it to Penn Central.

17. *Rules for Car Hire Settlement, supra,* p. 396.

18. *Chicago, R. I. & P. Ry. Co.* v. *U. S., supra,* pp. 91, 102; 49 U. S. C. § 15(8).

19. *Baltimore & O. R. Co.* v. *New York, N. H. & H. R. Co.,* 196 F. Supp. 724, 734 (S. D. N. Y. 1961).

and is entitled to offset such amounts (Jt. App. 39a); that Petitioners were required by law to participate in interline transportation with Penn Central and to permit it to use their cars (Jt. App. 45a); that such transactions gave rise to costs and charges [including their per diem balances] which were *not incurred as part of an ordinary debtor-creditor relationship*, and that Penn Central's estate is, therefore, impressed with an *equitable lien or trust* in such amounts (Jt. App. 45a, emphasis added). For relief, Petitioners and the railroads prayed for an order directing Penn Central to pay all such amounts or, in the alternative, for an order adjudging that these amounts represent equitable liens or trusts impressed upon all assets of Penn Central and are entitled to priority over all other secured or unsecured claims against Penn Central or its estate (Jt. App. 46a).

The Reorganization Court issued its opinion and Order No. 613 (A15) granting the Trustees' petition in part. The Court found that despite the railroads' obligation to interchange cars and otherwise deal with Penn Central, their claims for interline balances, including per diem and freight, arose out of a voluntary debtor-creditor relationship, in which the railroads voluntarily extended credit to Penn Central; and in such circumstances, giving consideration to the interests of other creditors and Penn Central, the Court declined to grant at that time any of the relief sought by the railroads and enjoined set off.

The Reorganization Court found that while the railroads were compelled by federal law to deal with Penn Central, there is no requirement that they extend credit to Penn Central. Referring to the proceedings leading to entry of Order No. 9, the Court recalled that the railroads there detailed measures (which were applicable only to the freight account—*not per diem*) "that could be taken to put a railroad, that could not be counted on to make its interline balance settlements, on a 'cash' basis" (A9). Moreover, the Court observed that other measures "could be used to put a railroad on a cash payment rather than a credit basis," citing "*Southern Ry. Co.* v. *Flournoy*, 301 F. 2d 847,

855-56 (4th Cir. 1962) (security deposit; creditor railroads' control of car movements)" (A9). Therefore, the Court stated, it was bound to follow *In re Central Railroad of New Jersey*, 273 F. Supp. 282 (D. N. J. 1967), aff'd *per curiam*, 392 F. 2d 589 (3d Cir. 1969) (the *CNJ* case);[20] thus, it rejected the railroads' "trust fund" argument for freight balances and, *sub silentio*, rejected the claim (in the Answer and Counterclaims) that the railroads are entitled to a declaration of constructive trust for their per diem balances. The Court, however, was not aware of the July 15, 1930 order of the Interstate Commerce Commission in the *Per Diem Rules* case, nor did it appreciate that, notwithstanding what self-help might be permitted for other interline accounts such as freight, railroads cannot lawfully compel settlement of per diem balances on a cash basis and have no means by which to protect themselves against non-payment of such balances. The Court, therefore, failed to distinguish this case, in which the railroads denied that per diem balances give rise to an ordinary debtor-creditor relationship, from the *CNJ* case, in which the parties conceded such a relationship. The opinion is silent on whether the Reorganization Court would have declared a constructive trust or equitable lien for per diem balances, or would have permitted set off, if the Court had found that self-help was not available for per diem balances and there was no voluntary extension of credit, and that such balances did not reflect an ordinary debtor-creditor relationship.

5. Opinion of the Court of Appeals.

The Court of Appeals reversed in part, holding that the freight and passenger revenues collected by Penn Central in behalf of other railroads are held in trust (A24) (to that extent rejecting the holding in *In re Central Railroad of New Jersey, supra*), and

20. In that case the parties conceded (*Id.*, p. 286) that the per diem transactions gave rise to a debtor-creditor relationship. Here, Petitioners claim that no ordinary debtor-creditor relationship arises from per diem transactions and that they are entitled to a declaration of constructive trust for per diem balances.

that such railroads are entitled to offset to the extent of such trust amounts (A44). The order of the Reorganization Court was in all other respects affirmed. With regard to the other interline accounts, including per diem, the Court of Appeals approved the reasoning of the Reorganization Court on the issue of self-help, and found that "there is no compulsion, statutory or otherwise, as to the manner by which the services shall be paid. Arrangements for payment or credit are voluntary." (A32-A33.) The Court of Appeals assumed, as did the Reorganization Court, that the railroads lawfully could have forced Penn Central on a cash basis for per diem. The Court was not aware of the Commission order in the *Per Diem Rules* case, or of the fact that the railroads are powerless to protect themselves against non-payment of per diem balances due them. Having concluded that the relationship of Petitioners to Penn Central was one of ordinary debtor and creditor, the Court did not consider that the Reorganization Court might declare a constructive trust in the amount of the per diem balances, or allow other relief, if it were to conclude that self-help was not available for per diem balances and there was no voluntary extension of credit, and that such balances did not reflect an ordinary debtor-creditor relationship.

REASONS FOR GRANTING THE WRIT OF CERTIORARI.

1. The Decision of the Court of Appeals Is in Conflict with a Decision of the Supreme Court.

In concluding that credit was voluntarily extended because "there is no compulsion, statutory or otherwise, as to the manner in which [per diem] shall be paid" (A32), the decision of the Court of Appeals is in conflict with the decision of this Court in *Chicago, R. I. & P. Ry. Co.* v. *U. S., supra,* which sustained the July 15, 1930 order of the Interstate Commerce Commission requiring that all railroads 100 miles or more in length "shall make car hire *settlements* direct with car owners in accordance

with the per diem rules." (A54-A56), emphasis added.) Under the Commission's order "settlement . . . in accordance with the per diem rules" requires uniform observance by all such railroads of Rules 11 and 12 of the Code of Per Diem Rules[21] and of the railroad practice, unvaried since before 1930, of settling per diem on a net balance basis by immediate draft.

Moreover, in concluding that the railroads could have used self-help to place Penn Central on a cash basis for per diem, and citing with approval *Southern Ry. Co.* v. *Flournoy, supra,* for the proposition that railroads can lawfully enforce a demand for "security deposit" and effectively "control car movements" (A33), the decision of the Court of Appeals is again in conflict with the decision of this Court in the *Rock Island* case. As this Court observed in the *Rock Island* case (at pages 91 and 102), a railroad cannot lawfully refuse to permit use of its cars by other roads. It is therefore powerless to enforce any demand not agreed to by the user. The suggestion to the contrary, in the decision of the Third Circuit in this case and of the Fourth Circuit in *Southern Ry. Co.* v. *Flournoy, supra* (at page 856, that a railroad can lawfully refuse to allow its cars to go on the lines of any road unwilling to guarantee the owner payment), should be expressly disapproved by this Court, as these decisions will affect decisions in other pending railroad reorganization proceedings under Section 77 of the Bankruptcy Act.

---

21. See footnote 13, *supra.*

2. A Determination by the Supreme Court of the Status of Pre-Reorganization Railroad Per Diem Claims and Whether Setoff or Other Relief Should Be Permitted, Is Necessary to the Proper Administration of Section 77 of the Bankruptcy Act in Conformity with Congressional Transportation Policy Embodied in the Interstate Commerce Act, Particularly Section 1(14)(a), and in the Last Sentence of Section 77(j) of the Bankruptcy Act.

The status of involuntary creditors generally, and of railroad per diem creditors in particular, in a reorganization under Section 77 of the Bankruptcy Act, presents an important—and timely—question of federal law which should now be decided by this Court. Also, this Court has not determined to what extent the operation of the Interstate Commerce Act, particularly Section 1(14)(a), should affect the status of pre-reorganization railroad per diem claims, nor has the Court determined whether railroad per diem claimants are involuntary creditors, having equity superior to voluntary creditors, and entitled to set off their claims or to a declaration of trust or equitable lien for such claims.

The principles applicable to the claims of voluntary creditors, like suppliers and banks, who may elect not to deal with a railroad or to deal only on conditions set by such creditors, should not be applied by a reorganization court to railroad claims for per diem, which arise from car interchange made mandatory by the Interstate Commerce Act, and for which no action can lawfully be taken to assure that payment of per diem will be made. This distinction also requires, particularly now when so much of the nation's rail plant is under the administration of reorganization courts, that this Court determine the equitable principles governing what relief should be granted to railroad per diem claimants.

For this proceeding, and for any other major railroad reorganization, the operation of the Interstate Commerce Act is the essence of the railroads' right to relief. The Interstate

Commerce Commission found, in the *Time-Mileage* case, that "the performance of orderly and efficient transportation service by rail in the future *requires the uniform observance of per diem charges by all railroads and* the *prescription of such uniform charges by this Commission pursuant* to the authority contained in *Section 1(14)(a)* of the Interstate Commerce Act . . .; that reasonable compensation to car owners *requires that the ownership costs be distributed among and borne equitably by all railroads making use of such cars in just proportion to the amount of use* . . .; [and] that reasonable compensation to car owners *requires the payment by all railroads of the time and mileage rate* set forth in Table C . . ."[22] (emphasis added).

Thus, by its very nature, "basic" per diem disclaims an ordinary debtor-creditor relationship. A cost-sharing joint venture,[23] compelled by federal law, is involved, with unique equities. There is no element of profit to the car owner, and the failure of any railroad to pay the prescribed compensation, distorts the equitable distribution of the cost of ownership of all per diem cars required by Section 1(14)(a) of the Interstate Commerce Act, by imposing upon the unpaid owners alone, in random amounts, the full burden of such non-payment. As per diem losses are not shared "equitably", failure of a railroad in reorganization to pay pre-reorganization per diem, or even the delay of such payment, violates the "reasonable compensation" premise of Section 1(14)(a). While non-payment of per diem may be required to sustain the objectives of Section 77 of the Bankruptcy Act, it should not be permitted except for the most compelling reasons. This Court should determine the principles which should govern a reorganization court's determination of whether to require payment of per diem or permit railroad per diem claimants to exercise the right of setoff or to grant them other equitable relief should non-payment be required for the ultimate success of reorganization.

22. *Chicago, B. & Q. R. Co.* v. *New York, S. & Western R. Co. supra,* pp. 258-259.

23. *Id.* p. 187.

Since railroads cannot refuse to permit use of their cars by other roads, before or during reorganization, and cannot protect themselves against non-payment of their per diem balances, their financial risk is unlimited and is assumed involuntarily, under compulsion of the Interstate Commerce Act. In the case of Penn Central, the magnitude of that risk is illustrated by the fact that the net payable balance in Penn Central's April 1970 Mileage and Per Diem Account was $12,358,000, that the total net payable balance for the period from May 1969 through May 1970 was $137,317,000, and that the average net payable balance was $10,563,000 per month in that period (Jt. App. 30a, Exh. D-1). It is doubtful that Congress intended that the Interstate Commerce Act should operate, in a reorganization proceeding under Section 77 of the Bankruptcy Act, to expose railroads to such financial risk, without adequate provision for relief. That the railroads are entitled to relief is suggested by Section 77(j) of the Bankruptcy Act[24] and by Section 1(14)(a) of the Interstate Commerce Act.

In addition to Penn Central, The Central Railroad Company of New Jersey, Lehigh Valley Railroad Company, and Reading Company, in the Third Circuit, Boston and Maine Corporation, in the First Circuit, Lehigh and Hudson River Railroad, in the Second Circuit, and Erie Lackawanna Railway Company and Ann Arbor Railroad Company, in the Sixth Circuit, are in reorganization under Section 77 of the Bankruptcy Act. The same issues as those involved in the instant case are presently pending in the Erie Lackawanna reorganization proceeding.

It is therefore of utmost importance to the proper administration of Section 77 of the Bankruptcy Act, in conformity with Congressional transportation policy embodied in the Interstate Commerce Act, particularly Section 1(14)(a), and in the last sentence of Section 77(j) of the Bankruptcy Act, that this Court determine the status of pre-reorganization railroad per diem claims and whether setoff or other relief should be permitted.

---

24. 11 U. S. C. § 205(j). In this section Congress has prohibited a reorganization court from enjoining or interfering with

CONCLUSION.

For the foregoing reasons, this petition for writ of certiorari should be granted.

Respectfully submitted,

RICHARD M. FREEMAN,
ZEV STEIGER,
400 West Madison Street,
Chicago, Illinois 60606,
Attorneys for Petitioners, Chicago and North Western Transportation Company, Grand Trunk Western Railroad Company and St. Louis-San Francisco Railway Company.

---

the right of a conditional vendor or lessor of railroad rolling stock to repossess such property in compliance with the provisions of its contract or lease, where the vendee or lessee is a railroad. This right to repossess operates to insure payment by the railroad of amounts due under such agreements, including pre-reorganization amounts, because default would result in loss of possession of the equipment. Although per diem claims do not arise under leases or other instruments protected by Section 77(j), the right to have them paid currently should be protected by the reorganization court for reasons at least as compelling as those operating to protect a lessor's right to have its rentals paid or to repossess, because railroads are compelled to permit the use of their cars by other roads, are entitled to payment under Section 1(14)(a) of the Interstate Commerce Act, and are powerless to protect themselves against non-payment.

APPENDIX.

IN THE UNITED STATES DISTRICT COURT
For the Eastern District of Pennsylvania

In Proceedings for the Reorganization of a Railroad.
No. 70-347

In the Matter of
PENN CENTRAL TRANSPORTATION COMPANY,
Debtor.

OPINION AND ORDER NO. 613.

[Re: Trustees' Petition to Compel
Payment of Interline Balances]

FULLAM, *J.* March 16, 1972

The Trustees have petitioned for an order directing certain rail carriers (interline railroads) to pay interline balances owing to the Debtor. The Trustees contend that these interline railroads have violated paragraph 10 of Order No. 1 in these proceedings, which provides in part:

> "All persons, firms and corporations . . . holding for the account of the Debtor deposit balances or credits be and each of them hereby are restrained and enjoined . . . from off-setting the same, or any thereof, against any obligation of the Debtor, until further order of this Court."

There is no substantial dispute that the interline railroads and the Debtor have claims against each other, nor is there any

substantial dispute as to the amount of these claims. The issues to be resolved herein, among others, are whether the claims of the interline railroads extinguish the Debtor's claims; assuming the Debtor's claims are not extinguished, whether the interline railroads are entitled to resort to the remedy of set-off against such claims; whether the interline railroads are entitled to an equitable lien on the estate of the Debtor for the amount of any claims remaining unpaid; and whether Order No. 9 in these proceedings requires additional payments to be made by the Debtor to the interline railroads.

I. The Factual Background.

A. *The System of Interline Accounts.*

The nation's railroads function in many ways as a single system. For example, a shipper or receiver pays one railroad for services of carriage for the entire shipment, although the shipment may travel over many different railroads; a railroad car may travel over the lines of many different railroads, and be used by each of them, before it again returns to the possession of the owning railroad; and a shipper whose freight may have been damaged in shipment by one of several carriers may apply to any of them for payment of his claim. The railroads have created a system of accounting and periodic settlement of accounts to facilitate this manner of operation. The accounting for various types of rail service rendered to the public or to other railroads results in "interline accounts," and the striking of balances between the railroads with respect to these interline accounts results in "interline balances." Each of the accounts is settled separately; there is no netting of the balances in different accounts.[1]

1. This system of accounts is established and governed by rules promulgated by the Association of American Railroads ("AAR"), of which the railroads in this proceeding are members. The "Rules" referred to in this Opinion governing each account and the publications in which they are found are listed in the Appendix.

The present petition involves six interline accounts; Freight, Passenger, Per Diem, Switching, Overcharge and Car Repairs. In addition, the respondents make reference to two other accounts: the Loss and Damage Account and an account encompassing "Miscellaneous Bills" for services, facilities and supplies furnished by one railroad to another. These accounts are described below.

Freight.

Where a freight shipment moves over more than one railroad, each road is entitled to be paid for the part of the carriage it performed. The destination carrier (who either collects from the consignee or debits the originating carrier if the shipment is prepaid) has the responsibility of computing from the waybill issued by the originating carrier the amounts due to the originating carrier and to the intermediate carriers. Rule 110A. These computations are made for each waybill reported by the destination carrier's agent in a particular month regardless of whether the freight charges have actually been paid.

The results of these computations ("abstracts" and "recapitulations of abstracts") must be sent to the other carriers by the 18th of the month following the month in which the waybill was issued. Rule 145. The Rule contemplates that at least the net figures should reach the other carriers by the 20th of that month. Rule 146. [The calculation of the account also may include corrections from freight accounts rendered as many as 36 months earlier. Rule 170.] After accounts are rendered, net balances are struck between the carriers. These balances are subject to immediate sight draft. Rule 149.

Passenger.

Interline passenger accounts are prepared by each ticket-selling carrier. The accounts so prepared are exchanged by mail on or before the last day of the month after the month in which the sales were reported. Rule 1. Here, too, settlement of the

net interline account balances is subject to immediate sight draft. Rule 9.

Overcharge.

The Overcharge Account reflects claims made by shippers for refunds in situations where too much was charged. A shipper may make such a claim against any carrier participating in the carriage. That carrier investigates the claim and pays it if it finds it valid. The paying carrier then charges the responsible carriers under the rules. These accounts are to be stated by the 10th of the month following the one in which the claim was settled; and settled by draft on or after the 25th of the same month on a gross basis. Rule 91A. It is the Debtor's policy to issue drafts against other carriers only for amounts it has actually paid to shippers.

Loss and Damage.

The same principles governing the Overcharge Account apply to the stating and settling of the Loss and Damage Account, Rule 152, except that the paying carrier must have actually paid before charges can be stated against another carrier. Rule 150.

Car Repair.

The National Safety Appliance Act mandates that each carrier perform necessary repairs on cars found to be defective. 45 U. S. C. A. § 13 (Supp. 1972). Bills for car repairs are required to be rendered no later than the last day of the month following the month in which the repairs were made. Each month's bill may include charges for car repairs made within the preceding 12 months. Settlement is made on a gross basis by draft on or after the 15th of the next month. Rule 23.

Per Diem.

The Per Diem Account reflects the daily rental charge for the use of railroad cars belonging to another carrier. Reports

of per diem due must be forwarded to the owning carrier by the 10th day of the second month following the month in which the per diem accrued. Rules 5, 6. The net balances of these accounts are subject to draft immediately thereafter.

Switching.

While the Switching Accounts are not governed by any mandatory rules, Freight Recommendatory Rule 408 sets forth the general intent of the industry concerning their settlement. It provides that the Switching Accounts that can be settled on a carrier-to-carrier basis (many apparently cannot) are to be stated by the 18th of the month following the month for which settlement is being made. Settlement is made by draft for the net balance due, not later than the 25th day of that month.

Miscellaneous Bills.

In addition to the transactions encompassed by the preceding accounts, interline railroads render bills to each other for such things as the joint operation of passenger terminals and freight yards, refrigeration services and the destruction of one railroad's equipment on another carrier's lines. These miscellaneous bills are settled by check. Disbursements Mandatory Rule 3 provides for the form of such bills; however, there are no general rules governing the time in which they should be rendered or paid.

B. *Proceedings Leading to the Present Petition.*

Paragraph 3 of Order No. 1 in these proceedings, entered June 21, 1970, the date Debtor filed for reorganization, provides in part:

> "The Debtor is authorized in its discretion, from time to time until further order of this Court, out of funds now in its possession or hereafter coming into its hands, to pay . . .
>
> "B. All other current expenses and costs hereafter necessarily incurred in operating, maintaining and preserving its railroad and other properties, collecting the revenues, and

> conducting the business of the Debtor . . . including . . . all wages . . . all interline accounts and balances owing by the Debtor . . . and all accounts for services, materials and supplies rendered or furnished to the Debtor."

The Debtor declined to pay any interline balances on or after June 21, 1970. On June 24, 1970, Burlington Northern, Inc. moved to amend Order No. 1 to require the Debtor to pay interline balances. A hearing was held on July 1, 1970, on that motion. At the conclusion of the hearing, the Court invited counsel to submit a form of order which would make mandatory the payment of post-petition interline balances stated from and after that date. That form of order became Order No. 9. The Court expressly left open the question of the status of the interline balances not required to be paid by that Order (Tr. 69).

II. The Merits.

The Trustees assert that the interline railroads have not paid amounts owing the Debtor under the applicable AAR Rules, for the six interline accounts mentioned above. As of the date of the hearing, November 29, 1971, it was undisputed that, apart from a few comparatively minor items in dispute, these interline balances amounted to approximately $3.4 million (Tr. 4064-65, 4068, 4077). The Trustees contend that the interline railroads are not entitled to set off their claims against this amount, and that the interline railroads should be compelled to pay the balances owing to the Debtor.

The interline railroads[2] make four responses to the Trustees' petition:

2. The term "interline railroads" as used in this Opinion refers collectively to the respondents to the Trustees' petition. The respondents have joined together in three groups: The Committee of Interline Railroads (the largest group); the Louisville and Nashville Railroad Company, and the three railroads joining with it; and the Indiana Harbor Belt Railroad. For the most part, the arguments made by one group are applicable to the others. Therefore, it will not generally be necessary to consider which group makes a particular argument.

Their first defense is in the nature of a counterclaim which, if sustained, would extinguish the claims of the Trustees. They assert that the Debtor owes them approximately $13.5 million and that the part of this amount attributable to the freight and passenger accounts must be considered a trust fund and that they are entitled to be paid that amount less what they owe the Debtor. While they do not contend that the other part of the $13.5 million which is attributable to the other interline accounts is a trust fund, they do contend that equitable principles entitle them to payment of this amount.

Second, the interline railroads contend that they are entitled to resort to the remedy of set-off against the claims of the Debtor. The Louisville and Nashville Railroad Company and the railroads joining with it expressly challenge the jurisdiction of this Court to enjoin set-offs against the Debtor's claims.

Third, the interline railroads contend that to the extent that their claims remain unpaid, they are entitled to an equitable lien on the estate of the Debtor.

Fourth, they counterclaim for amounts which they contend the Debtor is required to pay pursuant to Order No. 9 in these proceedings.

A. *The Right of the Interline Railroads to Payment of Their Claims.*

The interline railroads' first contention is that the amounts owed by the Debtor are trust funds. It is argued that pursuant to the Rules governing the freight and passenger accounts, the Debtor has collected money which belongs to the interline railroads and that these monies are "trust funds" which should be paid over to the interline railroads. Moreover, it is argued that because statutes and ICC regulations require the interline railroads to deal with the Debtor, the interline railroads' claims should be accorded a priority higher than the trade creditor who could choose whether or not to deal with the Debtor.

With respect to the trust fund argument, the interline railroads have cited various cases in support of the proposition that interline balances, representing the portion of monies collected by the Debtor for freight and passenger service performed by the interline railroads, are trust funds. However, two of the cases cited, *Atlantic Coast Line R. Co.* v. *Pennsylvania R. Co.*, 12 F. Supp. 720 (E. D. Pa. 1935); *Thompson* v. *Baltimore and O. R. Co.*, 80 F. Supp. 570 (E. D. Mo. 1948), *aff'd* 180 F. 2d 416 (8th Cir. 1950), hold only that where several railroads are involved in the carriage of a shipment and one of them, not in reorganization, has received payment for the entire carriage, the others may maintain an action in equity for their fair share. The exact nature of the revenues, *i.e.*, whether or not the revenues were "trust funds," was not an issue in either case. And the term was not used by either court as a basis of its holding but rather simply part of its analysis of the case as an action in equity. *Atlantic Coast Line R. Co.* v. *Pennsylvania R. Co., supra,* at 722-23; *Thompson* v. *Baltimore and O. R. Co.*, 80 F. Supp. at 572, 575; 180 F. 2d at 421.

In the third case relied on by the interline railroads, *Southern Ry. Co.* v. *United States,* 306 F. 2d 119 (5th Cir. 1962), the court based its statement that interline freight balances could acquire a " 'trust' character" "on a line of cases which hold [that] funds which have been wrongfully applied by the Court appointee during the pendency of a receivership, bankruptcy or reorganization," may become trust funds. *Id.* at 124-25, n. 5. This is obviously not the situation which is presented in this proceeding and, in any event, since the court in *Southern* ultimately determined that a priority should not be accorded to the interline balances under the trust fund theory, the court's statement can hardly be regarded as the holding of the case.

The interline railroads also assert that because they are compelled to deal with the Debtor, some special equities should arise in their favor. The interline railroads appear to assert in their memorandum of law that they were legally compelled to deal

with the Debtor so as to allow interline balances to become owing to them by the Debtor (Pp. 27-29, 38.)

While it is true that the interline railroads are required, for example, to accept from each other and to transport freight and passenger traffic and to correct unsafe conditions found on each other's cars, there is no requirement that interline railroads extend credit to each other. In fact, in proceedings leading to the entry of Order No. 9, the interline railroads detailed measures that could be taken to put a railroad, that could not be counted on to make its interline balance settlements, on a "cash" basis. *E.g.*, Tr. 23-26; Memorandum of Burlington Northern, Inc. (Document No. 18) at 5. Moreover, it is apparent that the interline railroads' description of such measures did not exhaust the list of measures that could be used to put a railroad on a cash payment rather than a credit basis. *See Southern Ry. Co.* v. *Flournoy*, 301 F. 2d 847, 855-56 (4th Cir. 1962) (security deposit; creditor railroads' control of car movements).

Therefore, the interline railroads having offered no persuasive authority to the contrary, this Court is bound to follow *In re Central Railroad of New Jersey*, 273 F. Supp. 282 (D. N. J. 1967). In that case, the arguments made here were presented, and the issues thus raised were resolved squarely against the interline railroads. The Third Circuit affirmed that decision *per curiam*, 392 F. 2d 589 (3d Cir. 1969), expressly adopting the district court's reasoning. Accordingly, I have concluded that the interline railroads are not presently entitled to payment of the pre-petition interline balances owed by the Debtor.

B. *Control of the Exercise of the Right of Set-Off.*

The interline railroads next assert that they should be accorded the right to offset their claims against the Debtor against the amounts they owe.

Having determined that equitable principles do not extinguish Debtor's choses in action running against the interline railroads, it is necessary to determine whether this Court can and should

enjoin the exercise of the remedy of set-off against those choses in action. The issue of this Court's jurisdiction to enjoin set-offs against choses in action held by the Debtor is no longer in question. *In the Matter of Penn Central Transportation Company, Debtor,* First Wisconsin National Bank, et al., Appellants, Nos. 19,340-19,346 (3d Cir., Dec. 23, 1971); *see In the Matter of Penn Central Transportation Company, Debtor,* Re: Application of the Trustees for an Order Directing Certain Shippers and Others to Pay Amounts Owing to the Debtor, Opinion and Order No. 571 (E. D. Pa., Jan. 31, 1972).

Whether set-offs should be enjoined presents a more substantial and more difficult issue. Many of the considerations discussed in the "shippers" case, above, are relevant here. The claims of the interline railroads arose out of transactions which were a vital part of the Debtor's day-to-day business. Such claims would probably fall within the so-called "six-months' rule" which has been held applicable in § 77 proceedings, and would likely be entitled to a high priority. *E.g.,* 5 *Collier on Bankruptcy,* ¶ 77.21 nn. 27-29 (1970).

But, just as in the "shippers" case, several factors persuade me that set-offs should be prohibited at this time. First, to permit set-offs could discriminate against the many other suppliers of services and equipment to the Debtor. At the hearing on July 1, it was estimated that pre-petition claims by these suppliers would aggregate over $200 million. In view of the substantial uncertainty that the interline railroads will be able to establish a distinction between their claims and the claims of the Debtor's trade creditors, it would not be appropriate to permit the interline railroads to resolve the question favorably to themselves through the self-help remedy of set-off prior to determination of the question in the proof of claims program.

Second, the Debtor's cash position must be considered. *See* the "shippers" Opinion, *supra* at 9. The Debtor is still unable to pay all of the costs of present operations, *e.g.,* taxes and leased-line rentals.

C. *The Claim for an Equitable Lien.*

The interline railroads' third contention is that they are entitled to an equitable lien on the Debtor's estate to the extent that their claims remain unpaid. The interline railroads argue, in essence, that even if they are not entitled to payment now on the basis of the various equitable theories discussed previously, at the least they should be entitled to an equitable lien. If this contention were sustained, it would be equivalent to the finding that the interline railroads are entitled to the payment of their claims from the Debtor's estate immediately after administration expenses, ahead of all other creditors.

The arguments that equitable principles entitle the interline railroads to immediate payment of their claims were rejected previously. But, whether an application of these principles should entitle the interline railroads to a priority, and what that priority might be, presents a different question. It appears, however, for a number of reasons, that decision of this question should await the classification of the interline railroads' claims in the proof of claims program. First, the Debtor's other creditors who may be affected by a decision of this question have not had an opportunity to express themselves with respect to it. Allowing an opportunity for such expression would be particularly important here where the interline railroads' entitlement to an equitable lien is open to serious question. Indeed, neither of the two cases cited by the interline railroads as directly supporting their contention, *In re Tennessee Cent. Ry. Co.*, 316 F. Supp. 1103 (M. D. Tenn. 1970), *Southern Ry. Co.* v. *Flournoy*, 301 F. 2d 847 (4th Cir. 1962), distinguished between claims of interline railroads and claims by trade creditors. Both cases dealt with the application of the six months' rule to claims of creditors, including interline railroads. Given the uncertainty of the proposition which the interline railroads advance, there can be no justification at this time for placing their claims ahead of the claims of the Debtor's trade creditors.

Second, whatever may be the situation in the reorganization of a smaller railroad, *Southern Ry. Co.* v. *Flournoy, supra* at 850, the classification of claims in this reorganization presents complex and difficult issues. Questions of this importance should be adjudicated in the context of the general program for determining the rights of creditors. For the two foregoing reasons, therefore, the application of the interline railroads for the imposition of an equitable lien on the estate of the Debtor will be denied without prejudice.

D. *The Counterclaim for Payment Under Order No. 9.*

The interline railroads' counterclaim is based on the contention that the Trustees have not paid all of the accounts which they were directed by Order No. 9 to pay. The pertinent language of the order requires payment of ". . . interline accounts and balances *first stated or presented and due to be stated or presented for settlement* on or after [July 1, 1970]." It is argued that this language requires payment of certain additional Car Repair, Passenger, and Miscellaneous Accounts which were or should have been billed before bankruptcy, but as to which sight-drafts were not due to be presented until after the date of Order No. 9.

This interpretation equates presentation of a draft and statement of the account; more importantly, it overlooks the word "first" in the Order. Accounts which were either stated or presented prior to the date of Order No. 9 were not required by that Order to be paid, and thus respondent's contentions with respect to the Car Repair and Passenger accounts are clearly without merit.

The Miscellaneous Bill Account presents different issues. The interline railroads assert that such bills aggregating approximately $1.9 million were, in normal course, first presented to the Debtor after the crucial date, and this fact is not substantially disputed. The question is whether this account was intended to be included in Order No. 9.

The Trustees argue that Order No. 9 relates only to accounts which are stated and settled in accordance with AAR Rules, and that the Rules do no govern settlement of Miscellaneous Bills, but only their form. Admittedly, however, the language of Order No. 9 can be more broadly interpreted.

It must be emphasized that the wording of Order No. 9 was drafted by counsel for the parties, by agreement. The Court was not called upon to rule, and did not consider, the specific application of the Order to the Miscellaneous Account. It now appears that the parties either did not consider this question, or at any rate are presently unable to establish that there was agreement on the question. Accordingly, a present decision as to the correct interpretation of Order No. 9 should be based upon the same considerations as if the underlying question were now presented to the Court for decision.

As discussed above, it can be persuasively argued that all of the claims of interline railroads should be treated no differently from the claims of trade creditors. Of all of the interline claims, the Miscellaneous Bills most nearly resemble the claims of ordinary trade creditors. I have therefore concluded that Order No. 9 should not be construed as requiring payment of the Miscellaneous Account claims which are the subject of respondents' counter-claims.

E. *Remedy.*

To summarize, I have concluded that the interline railroads are not now entitled to payment of their claims or to the declaration of an equitable lien or a priority in respect of them; that the counterclaims should be rejected; and that the interline railroads should be enjoined for the present from setting off these claims against the claims of the Debtor.

Pursuant to the practice followed in the "shippers" case, *supra*, an order in general terms will be entered at this time, on the assumption that implementation can be accomplished by further specific directions if necessary.

APPENDIX.

Source of Rules Governing Interline Accounts.

Freight Account: Freight Mandatory Rules in *Railway Accounting Rules* published by the Accounting Division, Association of American Railroads (effective Oct. 1, 1969) and its Supplement (effective Sept. 1, 1970) [hereinafter *"Railway Accounting Rules"*].

Passenger Account: Passenger Mandatory Rules in *Railway Accounting Rules.*

Overcharge Account: Overcharge Mandatory Rules in *Railway Accounting Rules.*

Loss and Damage Account: Freight Claim Rules published by Freight Claim Division, AAR (1970).

Car Repairs Account: Disbursements Mandatory Rules in *Railway Accounting Rules;* Code of Car Service Rules, Circular No. OT-10-B (effective Jan. 1, 1968), published by Operating-Transportation Division, AAR; Code of Rules for the Interchange of Traffic (effective Jan. 1, 1969), published by Mechanical Division, AAR and its Supplements Nos. 1 and 2.

Per Diem Account: Disbursements Mandatory Rules in *Railway Accounting Rules;* Code of Per Diem Rules Circular No. OT-10-B (effective Jan. 1, 1968), published by Operating-Transportation Division, AAR.

Switching Account: Freight Recommendatory Rules in *Railway Accounting Rules.*

Miscellaneous Bills: Disbursements Mandatory Rules in *Railway Accounting Rules.*

ORDER NO. 613.

AND NOW, this 16th day of March, 1972, it is ORDERED that:

1. The Petition of the Trustees for Order Directing Rail Carriers to Pay Interline Balances is GRANTED IN PART, and the respondents in this proceeding are enjoined, until further order of this Court, from setting off or attempting to set off against obligations due and owing to the Debtor on account of interline balances due in accordance with the Accounting Rules of the Association of American Railroads, any claim or claims which they may have against the Debtor for interline balances due from the Debtor in June or July, 1970, in accordance with said Accounting Rules, or other claims which arose prior to June 21, 1970, but any such claim or claims may be filed and proved in accordance with Order No. 164 in these proceedings. This Order shall be deemed to be without prejudice to the right of any such respondent to claim such priority as may be proper.

2. Order No. 9 in these proceedings does not require payment by the estate of the Debtor of bills from interline railroads for certain services, supplies and facilities referred to in the foregoing Opinion as "Miscellaneous Bills" and referred to in the "Memorandum in Support of Answer, Defenses and Counterclaims of the Committee of Interline Railroads . . ." as "Schedule A Accounts."

JOHN P. FULLAM, *J.*

UNITED STATES COURT OF APPEALS.
For the Third Circuit.

Nos. 72-1436, 72-1437, 72-1438

In the Matter of:

PENN CENTRAL TRANSPORTATION COMPANY,

Debtor.

Indiana Harbor Belt Railroad Company,

Appellant in No. 72-1436

Members of the Committee of Interline Railroads:

The Atchison, Topeka and Santa Fe Railway Company
Illinois Northern Railway
Burlington Northern, Inc.
Oregon Trunk Railway
Chicago, Milwaukee, St. Paul and Pacific Railroad Company
Chicago & North Western Railway Co.
Chicago, Rock Island & Pacific Railroad Co.
Peoria Terminal Co.
Delaware & Hudson Railway Co.
Greenwich & Johnsonville Railway Co.
Grand Trunk Western Railroad Co.
Kansas City Southern Railroad
Louisiana & Arkansas Railway Co.
Missouri-Kansas-Texas Railroad Co.
Missouri Pacific Railroad Co.
Texas & Pacific Railway Co.
Missouri-Illinois Railroad Co.
Chicago & Eastern Illinois Railroad
Norfolk and Western Railway Co.
New Jersey, Indiana & Illinois Railroad

Norfolk, Franklin & Danville Railway
Seaboard Coast Line Railroad Co.
Columbia, Newberry & Laurens Railroad Co.
Southern Pacific Transportation Company
San Diego & Arizona Eastern Railway
Northwestern Pacific RR
Portland Traction Company
Sunset Railway Co.
Visalia Electric Railroad Co.
St. Louis Southwestern Railway Co.
Southern Railway System
St. Louis-San Francisco Railway Co.
Alabama, Tennessee & Northern Railroad Co.
Quanah, Acme & Pacific Railway Co.
Union Pacific Railroad Co.
The Western Pacific Railroad Co.
Sacramento Northern Railway,

Appellants in No. 72-1437

Louisville and Nashville Railroad Company,

Appellant in No. 72-1438

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

Argued April 26, 1973

Before VAN DUSEN, ALDISERT and ROSENN, *Circuit Judges*

Reargued before the Court En Banc May 23, 1973

Present: VAN DUSEN, ALDISERT, ADAMS, GIBBONS, ROSENN and WEIS, *Circuit Judges*

W. Charles Hogg, Jr., Esquire
Edward C. Toole, Jr., Esquire
Clark, Ladner, Fortenbaugh and Young
William R. Glendon, Esquire
Frederick W. R. Pride, Esquire
William J. O'Brien, II, Esquire
George W. Brandt, Jr., Esquire
Royall, Koegel & Wells
for appellants

Paul R. Duke, Esquire
Richard R. Bongartz, Esquire
for appellee

OPINION OF THE COURT.
(Filed October 9, 1973)

ROSENN, *Circuit Judge.*

The primary issues raised on this appeal are (1) whether freight and passenger revenues earned by railroad carriers for interline transportation or services but collected by Penn Central Transportation Company (Penn Central) in their behalf are held by it as trust funds, and (2) whether other interline services performed and expenses incurred by the interline carriers for Penn Central prior to its reorganization are entitled to current payment or offset. The district court in Penn Central reorganization held that the interline railroads[1] (Interlines) were

1. An "interline railroad" is a railroad common carrier which cooperates with other railroads in the transportation of passengers or property over their lines, as required of all railroads engaging in interstate commerce by the Interstate Commerce Act. 49 U. S. C. § 1(4). The act provides in relevant part:

> It shall be the duty of every common carrier subject to this chapter to provide and furnish transportation upon reasonable request therefor, and to establish reasonable through routes with

not entitled to current payment of their claims from the debtor or to a declaration of an equitable lien or priority. In addition, the court enjoined them from setting off these amounts against corresponding claims of Penn Central. In reviewing this order we are compelled to examine the complex accounting procedures of our national railroad systems and apply traditional principles of equity and trust law to the operating relationship among the railroads. We affirm in part and reverse in part.

I. The Background.

The district court has succinctly described the system of accounts of interline railroads in its Opinion and Order No. 613 (E. D. Pa., No. 70-347, dated 3/16/72) as follows:

> The nation's railroads function in many ways as a single system. For example, a shipper or receiver pays one railroad for services of carriage for the entire shipment, although the shipment may travel over many different railroads; a railroad car may travel over the lines of many different railroads, and be used by each of them, before it again returns to the possession of the owning railroad; and a shipper whose freight may have been damaged in shipment by one of several carriers may apply to any of them for payment of his claim. The railroads have created a system of accounting and periodic settlement of accounts to facilitate this manner of operation. The accounting for various types of rail service rendered to the public or to other railroads results in "interline accounts," and the striking of balances between the railroads with respect to these interline accounts results in "interline balances." Each of the accounts is settled separately; there is no netting of the balances in different accounts.[1]

---

other such carriers, and just and reasonable rates, fares, charges, and classifications applicable thereto; . . .

See, e.g., Southern Ry. Co. v. Flournoy, 301 F. 2d 847, 854 (4th Cir. 1962).

1. This system of accounts is established and governed by rules promulgated by the Association of American Railroads ("AAR"), of which the railroads in this proceeding are members. . . .

The methods of accounting and payment for interline services, however, are not controlled by statute but by industry accounting practices and rules.

The two basic categories of accounts here in issue are: (1) freight and passenger accounts; (2) other accounts, including (a) car repair accounts, (b) overcharge and loss and damage accounts, (c) per diem accounts, and (d) switching accounts. The accounting rules, described below in greater detail, differ for each of the categories. Basically, as to the first category, either the destination or the originating carrier collects the sums earned by each of the interline railroads and then allocates the appropriate amounts. As to the other accounts, the railroad that performs the service collects the amounts due it from the appropriate carrier.

Penn Central filed its petition for reorganization under section 77 of the Bankruptcy Act on June 21, 1970. In Order No. 1, approving the petition, entered on the same day, the court in paragraph 3(B) authorized Penn Central "in its discretion" to pay all interline accounts.[2]

On June 24, 1970, one of the interline carriers, Burlington Northern, Inc., petitioned the district court to require Penn Central to pay interline accounts and balances.[3] At a hearing

2. The order stated that Penn Central was authorized to pay all interline accounts and balances owing by Debtor, including amounts in respect of revenues from freight, passenger or other traffic interchanged with other carriers, and charges for repairs of, or loss damage to, rolling stock and equipment interchanged with other carriers, all claims for injuries, death or other loss or damage to passengers and others arising from the operation of its railroad and properties, and all claims for loss, damage or delay to freight and baggage and all claims for overcharges and for reparation, and all accounts for services, materials and supplies rendered or furnished to the Debtor, whether chargeable in the first instance to expenses, or otherwise.

3. The "interline carriers" involved in this appeal are the 39 railroad systems set forth in the caption of this opinion. All appellants except the Indiana Harbor Belt Railway Company and the Louisville and Nashville Railroad Company intervened in the proceeding below as the Committee of Interline Railroads. The Committee includes 40 additional railroads not here involved.

on July 1, 1970, Charles S. Hill, Penn Central's Vice-President-Comptroller, explained that Penn Central incurs an average net liability for interline charges of $24 million per month, owing $41 million and earning $17 million. On accounts stated in June 1970 which remain unpaid and are here in issue, he said it owed approximately $32.8 million, representing services performed in April and May 1970, and earlier.

Mr. Hill also endeavored to explain Penn Central's plans as they related to interline accounts. He described Penn Central's cash forecast for the month of July and, when asked whether interline balances had been provided for, replied:

> We have made provision on the expectation with the approval of the Court for meeting all of the interline accounts to be presented after or scheduled to be presented after June 30.

He explained that these payments would reflect services performed in June 1970 and earlier and that payment on them would begin July 23.

At the conclusion of the hearing, the court invited the parties to submit an order making mandatory the payment of charges stated "from and after" July 1, 1970. Order No. 9, drafted by the parties, was entered the same day. It ordered the payment of all interline accounts first stated or presented on or after July 1, 1970.[4] It also specifies that it does not prejudice

4. The relevant portion of Order No. 9 states:

> And Now, to wit: this First day of July, 1970, it is HEREBY ORDERED that paragraph 3 of the Order of June 21, 1970, is hereby AMENDED so as to direct and require the Debtor (in lieu of authorizing the Debtor in its discretion) to pay to other railroads freight charges and divisions, passenger or ticket charges and divisions, per diem, mileage, and per diem claims, car repairs, trailer rentals *and all other interline accounts and balances first stated or presented and due to be stated or presented for settlement on or after the date of this Order* in accordance with the now existing rules and procedures of the Association of American Railroads and otherwise in accordance with the rail carriers' ordinary business practice. [Emphasis supplied.]

the right of the Interlines to claim priority for interline accounts stated prior to July 1.

A controversy subsequently arose when the Interlines attempted to set off the interline balances they owed Penn Central against amounts owed them by Penn Central. Consequently, on June 24, 1971, the trustees petitioned the court to order that the Interlines pay all balances due. The trustees alleged that the Interlines had failed to honor drafts drawn by Penn Central in total amount of $413 million representing pre-bankruptcy interline balances such as claims for May 1970 freight services.[5] They contended that this violated Order No. 1, paragraph 10, providing:

> All persons, firms and corporations . . . holding for the account of the Debtor deposit balances or credits be and each of them hereby are restrained and enjoined from selling, converting or otherwise disposing of such collateral, deposit balances or other credits or any part thereof, or from offsetting the same, or any thereof, against any obligation of the debtor, until further order of this court.

The Interlines defended and counterclaimed, alleging that they were entitled to offset amounts they owed Penn Central against amounts Penn Central owed them. They also alleged that Penn Central held in trust for them (a) amounts collected in their behalf for interline freight and passenger services and (b) amounts they paid on Penn Central's behalf for overcharge and loss and damage claims. In addition, they argued that Penn Central's assets should be impressed with an equitable lien for such amounts. In counterclaiming, they further alleged that Order No. 9 required Penn Central to pay immediately unpaid interline balances which would become subject to draft in July and represented pre-June 20 car repairs, passenger receipts, and services and supplies.

The district court ruled in favor of the trustees and entered Order No. 613 enjoining any further setoffs. The Interlines

5. The parties have indicated that these amounts are primarily May 1970 freight and passenger balances.

appeal that order. They argue (1) that Penn Central holds in trust balances arising from freight and passenger services rendered by the Interlines; (2) that other interline accounts must be paid because the Interlines are compelled by law to perform these services; and (3) that Order No. 9 requires the payment of May 1970 car repair charges and passenger balances which become subject to draft in July.

II. Freight and Passenger Accounts.

Freight and passenger charges are collected by the originating or destination carrier for services performed by the Interlines. Under the AAR rules, instead of separately paying each carrier that participates in an interline shipment, the shipper pays all freight charges to either the originating carrier when the shipment is "prepaid" or to the destination carrier on "collect" shipments. Funds collected are deposited in the collecting carriers' general accounts. The interline railroads make numerous collections for each other daily which are segregated and settled monthly. No interest is paid by the collecting carrier for the period it holds another carrier's revenue.

The destination railroad is responsible for preparing and settling interline freight accounts. It prepares an "abstract" on which the appropriate freight charges are allocated to the participating carriers. It then "not later than the eighteenth of the succeeding month" sends copies of the abstract to the other carriers.[6] The carriers may then *immediately* draw a draft on the destination railroad for the *net balance* due for the month. The destination carrier must include in the monthly accounting all charges for which the destination carrier has received a waybill, whether or not the shipper paid. The waybill is issued by the originating carrier and prescribes the movement of the

6. If the settling carrier is unable to forward the interline freight summary in time to reach the other carriers by the twentieth of the month, upon request, it must notify the carriers by prepaid telegram. Thus, freight balances are subject to draft, at the latest, on the twentieth.

shipment and charges. The charges which Penn Central has not paid in the instant case represent May 1970 freight services; Penn Central declined drafts submitted on or after June 22, 1970, of approximately $15 million for these accounts.

Passenger accounts are handled similarly. The monthly reports, however, are not required until the last day of the first month following the service. Net passenger balances also are subject to immediate draft upon receipt of the statements. Penn Central has declined drafts submitted on or after July 1, 1970, for approximately $280,000 for May traffic.

The AAR interline accounting system is in essence, therefore, a system by which one railroad collects monies owed by shippers to both itself and other railroads. The monies collected belong only in part to the collecting railroads; as to monies owed other railroads, the collecting railroad serves merely as a receiving and transmitting agent. A common sense interpretation of this system would indicate that funds collected by one railroad for and in behalf of another railroad are held in trust by the collecting railroad until the monies are transmitted. Whether the money is held in trust must be determined, however, not merely by reliance on common sense, but also by application of traditional legal doctrines. We therefore turn to the law of trusts to make that determination. In applying the law of trusts, it will be necessary to examine the manifestation of intent of the parties, not only in terms of written documents, but also in terms of the conduct of the parties. Especially important in the present case are (1) the absence of any payment of interest on monies collected during the time they are held by the collecting railroad, and (2) the commingling of the monies with general funds by the collecting railroad.

Accommodating and applying traditional common law trust principles to the unique regulatory scheme and accounting policies used by the nation's railroads, we have concluded that transportation and freight charges, *when collected,* are held in trust for the Interlines. They are therefore entitled to have their monies immediately.

A trust is defined in *Restatement (Second) of Trusts* § 2 (1959) as:

> [A] fiduciary relationship with respect to property, subjecting the person by whom the title to the property is held to equitable duties to deal with the property for the benefit of another person, which arises as a result of a manifestation of an intention to create it.

The parties' manifestation of intention ultimately controls whether or not a trust relationship exists, but failure to expressly designate the relationship as one of trust does not necessarily negate its existence. *See United States* v. *Orsinger*, 428 F. 2d 1105, 1112 (D. C. Cir. 1970); *Del Drago* v. *Commissioner*, 214 F. 2d 478, 480 (2d Cir. 1954); *State* v. *United States Steel Co.*, 12 N. J. 51, 95 A. 2d 740, 744 (1953); 1 *A. Scott, Law of Trusts* § 2.8 (1967). When the language of the parties fails to clearly indicate their intention, it may be ascertained by other objective manifestations of intent, such as the facts and circumstances surrounding the transaction and the relationship of the parties. *Stratford Financial Corp.* v. *Finex Corp.*, 367 F. 2d 569, 571 (2d Cir. 1966); *In re Chicago Express, Inc.*, 222 F. Supp. 572 (S. D. N. Y. 1963); 1 *A. Scott, supra*, § 12.2, at 108.

A significant fact in the instant case warranting careful consideration is the absence of any provision for the payment of interest by the collecting carrier. Although not conclusive, its absence indicates the presence of a trust relationship. *See United States* v. *Orsinger, supra; State* v. *Atlantic City Electric Co.*, 128 A. 2d 861, 865-66 (1957); *State* v. *United States Steel Co., supra.* A debtor-creditor relationship entails the right to use another's money, the usual quid pro quo for which is the obligation to pay interest. *See* 1 *A. Scott, supra*, § 12.2, at 108. Conversely, the collection by Penn Central as an agent of money due and owing the other railroads suggests a trust. *See, e.g., In re Chandler Insurance Agency, Inc.*, 92 F. Supp. 878 (D. Md. 1950); *National Indemnity Co.* v. *American National Bank*, 120 F. Supp. 713 (D. Minn. 1954), *aff'd*, 222

F. 2d 513 (8th Cir. 1955); *Restatement (Second) of Trusts* § 12, comment h (1959).

On the other hand, appellee trustees argue forcefully that the Interlines, by permitting Penn Central to commingle monies due them with Penn Central's general revenues, established a debtor-creditor relationship and not a trust. While generally commingling indicates a debtor-creditor relationship and not a trust, it is only one indicium and it too is not necessarily conclusive. *See National Bank* v. *Insurance Co.*, 104 U. S. 54, 68 (1881); *MacBryde* v. *Burnett*, 132 F. 2d 898, 900 (4th Cir. 1942); *State* v. *United States Steel Co.*, 12 N. J. 51, 95 A. 2d 740, 744 (1953).

Commingling of monies has minimal significance in the extraordinary operations of interline railroads. That Penn Central is not, as a destination carrier, required by the other carriers to immediately segregate funds collected does not necessarily reflect any intention to establish a debtor-creditor relationship in the face of the unique and complex interline railroad system. Normal operation conditions with innumerable daily collections of various categories preclude practically and economically any effective daily segregation. Burlington Northern Railway alone has more than 1300 stations from which waybills are issued.[7] This is not a simple situation of one party receiving money clearly designated as payment for services performed by another. When a carrier collects funds for another railroad, it does not immediately know what portion of the revenues collected is to be allocated to other carriers.

---

7. The affidavit of Assistant Vice President Wigstrom of Burlington Northern, Inc., asserted:

> [A]t more than 1300 stations must transmit to the Company's general offices (through three regional customer accounting centers) the waybill for each shipment terminated at their respective stations. The waybill data for every terminated interline shipment must, as noted by Mr. Bergey, be abstracted in order to prepare the interline settlement statement. The settlement of interline accounts cannot be achieved either practically or economically among the nation's railroads on anything approaching a daily basis.

Mr. Hill, Penn Central's Vice-President-Comptroller, testified that Penn Central settles regularly with more than 300 interline carriers. Settlement involves calculating amounts due each carrier for many different waybills sent daily to Penn Central. We recognize the enormous difficulties confronting the destination carrier to correlate each of these waybills with payments received on a monthly basis, not to mention daily basis, and to segregate funds received according to the waybills.

AAR rules merely serve to evidence the necessities of the situation. To accommodate the carriers in this exceedingly voluminous and complicated accounting system, the AAR rules require that the statements be rendered only once each month and give the carriers 18 days to prepare the abstract of the interline freight accounts after the end of the month in which the waybill is received. The rules also indicate the difficulty in segregation of collections. They require that accounts may be drawn on the collecting carrier after the specified period even though in some instances the charges have not yet been collected from the shippers.[8]

Each party in this controversy finds support for its position in a number of cases that specifically concerned interline accounts. Although we think none are directly in point with this case,[9] none rebut our conclusion that the freight and transportation collections are held in trust.

---

8. The 18-day period, in addition to facilitating accounting, preserves the fairness of the nonsegregation because most of the charges have been collected by the time of the drafting date.

9. The Interlines rely on Morgenthau v. Sugarland Railway Company, 83 F. 2d 72, 74 (5th Cir. 1936); Baltimore & Ohio R. R. Co. v. Thompson, 80 F. Supp. 570, 586 (E. D. Mo. 1948), *aff'd*, 180 F. 2d 416 (8th Cir. 1950); and Atlantic Coast Line Railroad v. Pennsylvania Railroad Company, 12 F. Supp. 720 (E. D. Pa. 1935), to support their contention that the passenger and freight account monies were held in trust. Although there is dicta in each of those cases indicating that such funds collected by an interline carrier are held in trust, we do not rely extensively on that dicta, because the issue of whether or not a trust existed was not squarely presented to the court in any of the cases.

In *Southern Railway Company* v. *United States*, 306 F.2d 119 (5th Cir. 1963), the court refused to accord priority to interline claims of the Southern Railway against the receiver of the Tallulah Falls Railway Company for amounts earned by Southern or paid by Southern to other carriers and collected by the receiver. According to the court, the freight payment first became in arrears in June 1958, and the receiver repeatedly advised Southern that it was unable to make the payments. Nonetheless, Southern made no demand for segregation of monies collected for it until May 1960. The court declined on a "laches" theory to accord the interline claims priority. It reasoned that Southern knew of the precarious financial situation of the railroad in receivership but continued to disburse its own funds to prior connecting carriers "with full awareness that the funds were not being reimbursed by the Receiver and that, as with routine day-to-day operating charges, the Receiver was using its money, its supplies, and its facilities on which to run the Railroad." *Id.* at 125.

The Interlines in this case, however, were not guilty of such folly. They began demanding payment within three days of filing the reorganization petition. *Southern Railway*, moreover, does contain dictum indicating that, aside from the laches problem, the court indicated the funds collected acquired a trust character at the time the accounts were presented.[10] The court stated:

---

10. The settlement procedure in *Southern* was similar to that in this case. The court described it as follows:

> The two carriers had a junction settlement arrangement under which freight interchanged was re-billed at Cornelia. On traffic moving inbound to the Tallulah Falls, Southern paid all prior participating carriers their divisions or proportions of the revenue for traffic handled over their lines. For these advances as well as for its own division or proportions of the inbound freight charges, Southern looked to the Receiver for reimbursement and payment. As to such inbound shipments, the Receiver would, and did, collect the freights from consignees. On movements out-bound from the Tallulah Falls, the destination carrier collected the freight charges and paid over to Southern the share

> The Receiver had a right to collect and to *retain*. The duty to remit was limited to the balance when and as struck in the periodic settlements. Only then did funds, rightfully collected and mingled, acquire a "trust" character.

306 F.2d at 125. Applying this statement to the case sub judice, the freight accounts for the month of May 1970 acquired a trust character when stated on June 18, 1970.

In re Chicago Express, Inc., 222 F. Supp. 566 (S.D. N.Y. 1963), *aff'd*, 332 F.2d 276 (2d Cir. 1964), *cert. denied*, 379 U.S. 879 (1964), involved a claim by the Pennsylvania Railroad Company for priority in the bankruptcy of a trucking company. By agreement, Pennsylvania carried trailers of the motor carrier "piggy-back" on flat cars. Pennsylvania's charges for this service depended on several variable factors, including the number of trailers transported during a given month, the weight of the trailers, and the distances traveled. The railroad's charges were not related to the trucker's charges to its customers; the Pennsylvania made no inquiry into customer charges. The trucking company was obligated to pay within 15 days from the date of billing by Penn Central. This 15-day period was referred to by the parties in their rate agreement as a "credit accommodation" and was subject to suspension if payment was not timely. In rejecting the Pennsylvania's argument that proceeds received by the trucker from its shippers to the extent attributable to "piggy back" hauls constituted trust funds held for Pennsylvania, the court explained,

> The following are some of the facts which lead me to conclude, as did the Referee, that the relationship between the parties here was one of creditor and debtor, and not trustee and beneficiary: the absence of an agreement between the Pennsylvania and the Debtor to apportion total charges; the lack of relationship between the amount due

---

due it as well as the Tallulah Falls. The settlement arrangement called for adjustment four times a month. On striking the balance, payment was to be made by, or to, the Receiver or Southern as the case might be.

306 F. 2d at 123.

> the Pennsylvania from the Debtor and the overall charge made by the Debtor to its customer; the unconditional duty of the Debtor to pay freight charges to the Pennsylvania within fifteen days from the day of billing, and the "credit accommodation" clause in the "divisional sheet."
>
> 222 F. Supp. at 572

These facts in *Chicago Express* clearly differentiate it from the case sub judice. Penn Central did have an arrangement with the Interlines to apportion total charges; the amounts received by the Interlines were directly related to and dependent upon charges paid by shippers; and the amounts owed to the Interlines were payable immediately upon striking the monthly settlement.

Penn Central argues, however, and the district court agreed, that this issue was previously settled in *In Re Central Railroad of New Jersey*, 273 F. Supp. 282 (D.N.J. 1967), *aff'd per curiam*, 392 F.2d 589 (3d Cir. 1968). It is true that in that case the district court held that the New York Central Railroad Company (NYC) could not set off amounts it owed the Central Railroad of New Jersey (Central) for post-reorganization freight transportation against amounts owed by Central to it for pre-reorganization freight transportation by NYC. In reaching that result, the court concluded that the amounts collected by Central for NYC's interline service were not trust funds. 273 F. Supp. at 288. We affirmed by a per curiam opinion. To the extent the *Central Railroad* decision is inconsistent with the case sub judice, it should not be followed.

The concurring opinion expresses concern because of our reliance upon established principles of trust law which may in some future case, when possibly "the traditional indicators of a trust relationship" are absent, require a contrary holding and thus might disrupt interline railroad transportation. The principal problem before us is one of accounting for funds belonging to another, readily resolvable by recognized trust and pragmatic considerations to which we have alluded. These principles

are appropriate to any industry, regardless of their operational problems, and our decision supports the congressional policy encouraging interline rail transportation of freight and passengers nationwide. We perceive no need to announce an entirely new and necessarily result-oriented rule of law which is not pertinent to our present decision, merely because of the fear that the traditional approach may be restrictive in some future unstated hypothetical situation.

III. Other Interline Accounts.

The AAR accounting system and contractual obligations for the interline accounts other than those for freight and passenger carriage present different problems. In order to ascertain whether setoffs should be allowed as to Penn Central liabilities on these accounts, it is necessary to examine them seriatim.

Car Repairs. The Interlines frequently repair the equipment of other connecting carriers under the requirements of the National Safety Appliance Act, 45 U. S. C. § 13. AAR rules direct the rendition of bills for repair work no later than the last day of the following month. A draft for payment may be drawn on or after the fifteenth of the second following month.

Overcharge and Loss and Damage Accounts. When a shipper finds too much has been charged by the railroads, or that he is due payments for loss of, or damage to, the goods shipped, he makes a claim to any carrier which participated in the shipment. That carrier investigates the shipper's claim, makes whatever payment is necessary, and then charges the responsible carrier. Accounts are stated on the 10th of each month for all shipper overcharge claims finally settled and all shipper loss and damages claims actually paid. The carrier which has paid the claim may then draw a draft on the responsible carrier on or after the 25th day of the same month.

Per Diem Accounts. When one railroad uses the cars of another railroad, it pays that carrier a daily rental. Reports of

amounts owed are forwarded to the owing carrier by the 10th day of the second month following use of the car. The net balances of these accounts are subject to immediate draft.

Switching Accounts. When one railroad switches a car for the benefit of another railroad, a switching charge is made. Such charges for cars moving in interline shipments are computed by the destination carriers and then sent to the Interlines no later than the 18th day of the month after the charges were incurred. Settlement is on the 25th day of that month.

We have concluded that amounts due on these accounts are not held in trust. These accounts do not involve collection of money by one carrier for another. These accounts merely represent the performance of services by one railroad. Although no interest was paid to Penn Central, no accounts except for the per diem balances were subject to immediate draft as were the freight and passenger accounts. Therefore, as to these accounts, the Interlines at this juncture are in exactly the same position as other suppliers of Penn Central who were unpaid for goods and services delivered prior to the filing of the reorganization petition.

The Interlines argue that these amounts must be paid immediately because the accounts "arise directly from specific statutory requirements and are absolutely essential to the operation of a national rail transportation system." They argue that they are compelled (apparently by 49 U. S. C. § 1(4)) to permit use of their box cars by Penn Central and other carriers. Similarly, the National Safety Applicance Act, 45 U. S. C. § 13, requires that they repair Penn Central's cars if they break down on their tracks. They argue that a destination carrier is required by law to process claims for damage to goods in transit and to advance monies to discharge or settle the claim.

Despite the legal obligation to perform the services, there is no compulsion, statutory or otherwise, as to the manner by which the services shall be paid. Arrangements for payment or

credit are voluntary.[11] Most important, however, is the recognition that no money is collected as to these accounts by Penn Central for other railroads.

The overcharge, loss, and damage accounts present a more difficult problem conceptually. Nevertheless, the essential basis for a trust does not exist. AAR practices call for one carrier to advance sums on behalf of other carriers when valid claims are made by shippers. Such advances are, in effect, a service one carrier renders for other carriers, similar to the services the Interlines perform for each other in renting and repairing cars. In a sense, if the Penn Central receives payment for a shipment, part of which eventually has to be repaid to the shipper, it could be argued that Penn Central in the interim holds the sums in trust to return to the paying carrier. However, at the time Penn Central originally received the freight payments, it had no notice that at a later date part of those sums would have to be returned. Any overcharge, loss, or damage claims at that time would be inchoate and amorphous. The relationship between the advancing carrier and the liable carrier is thus much closer to that of debtor-creditor than that of trustee-beneficiary.

Previously, we upheld the reorganization court's authority to prevent banks from using the self-help remedy of setting off amounts owed them by Penn Central against their obligations

11. The district court properly reasoned:

> While it is true that the interline railroads are required, for example, to accept from each other and to transport freight and passenger traffic and to correct unsafe conditions found on each other's cars, there is no requirement that interline railroads extend credit to each other. In fact, in proceedings leading to the entry of Order No. 9, the interline railroads detailed measures that could be taken to put a railroad, that could not be counted on to make its interline balance settlements, on a 'cash' basis. *E.g.*, Tr. 23-26; Memorandum of Burlington Northern, Inc. (Document No. 18) at 5. Moreover, it is apparent that the interline railroads' description of such measures did not exhaust the list of measures that could be used to put a railroad on a cash payment rather than a credit basis. *See* Southern Ry. Co. v. Flournoy, 301 F. 2d 847, 855-56 (4th Cir. 1962) (security deposit; creditor railroads' control of car movements).

to Penn Central. *In re Penn Central Transportation Company*, 453 F. 2d 520 (3d Cir. 1971) (the *Bank Cases*). Similarly, we have upheld its authority to enjoin shippers from setting off amounts Penn Central owed them for freight loss and damage claims against amounts they owed Penn Central for freight services. *In re Penn Central Transportation Company*, Nos. 72-1436 to 1438 (3d Cir. 1973) (the *Shipper Cases*).

In the *Shipper Cases*, we explained: (1) Under the Interstate Commerce Act, 49 U. S. C. §§ 3(1) and 6(7), freight charges are accorded a preferred status and are not subject to the defense that the carrier owes the shipper money for other items. We noted that the only defense that can be raised to a carrier's suit for freight charges is "that the services have been paid for, that the services were not rendered, that the services were charged under an inapplicable tariff schedule, or that the rates were unreasonable." .....F. 2d at ..... (2) Although a shipper nevertheless retains a right to assert a counterclaim in a carrier's suit for freight charges, *Chicago & Northwestern Railway* v. *Lindell*, 281 U. S. 14 (1930), that right is extinguished by the intervention of a railroad reorganization proceeding. (3) Since the shippers' claims did not have the legal status of defenses, they cannot defeat "the right of the railroad to collect absolutely all legal charges for freight services outstanding and unpaid."

In the *Bank Cases*, we reasoned that permitting creditors to refuse to pay their obligations because Penn Central owed them similar amounts would place them in a preferred position over other creditors and endanger the success of the reorganization. We noted: "Even secured creditors of a railroad must submit to the risk inherent in judicial suspension of the rights they normally would have to enforce their liens against property of the debtor during the pendency of a reorganization proceeding. New Haven Inclusion Cases, 1970, 399 U. S. 392 [1970]." 453 F. 2d at 523.

In this case, we reaffirm the reorganization court's authority to preclude setoffs. The threat to the reorganization that we noted in the *Bank Cases* is present in the assertion of these setoffs. Penn Central's choses in action for the various interline charges are entitled to the same status as the freight charges in the *Shipper Cases* and the deposits in the *Bank Cases*. The district court concluded that to permit setoffs could discriminate against many other suppliers of services and equipment and would be unfair because of the unresolved issue of the relative priorities of the claims. It also concluded that Penn Central's cash position would be unduly injured by allowing the setoffs.

In the absence of a trust relationship, whether to permit a setoff is in the discretion of the district court. *See Susquehanna Chemical Corp.* v. *Producers Bank & Trust Co.*, 174 F. 2d 783, 786-87 (3d Cir. 1949). We find no abuse of discretion in the circumstances of this case.

For the foregoing reasons, the interline railroads may not set off their claims, except for freight and passenger accounts, against amounts owed by them to Penn Central. The freight and passenger claims are entitled to different treatment because of their trust character and the Interlines resulting right to immediate payment regardless of the reorganization.

IV. The Effect of Order No. 9.

Order No. 9 requires Penn Central to pay all interline accounts "first stated or presented for settlement on or after [July 1, 1970]." Appellants argue that Penn Central's failure to pay for May 1970 car repairs, which became payable on or after July 1, violates the order.[12] The district court rejecting appellants' argument reasoned:

12. Appellants also make this argument as to passenger accounts, but since we have concluded that the passenger receipts are held in trust, we need not specifically discuss their status under Order No. 9. In the district court, appellants also asserted that unpaid miscellaneous bills were required to be paid by Order No. 9, but they do not press this contention on appeal.

> This interpretation equates presentation of a draft and statement of the account; more importantly, it overlooks the word "first" in the Order. Accounts which were either stated or presented prior to the date of Order No. 9 were not required by that Order to be paid, and thus respondent's contentions with respect to the Car Repair and Passenger accounts are clearly without merit.

We agree with the district court.

Appellants argue that the parties drafted the language of the order and that the testimony at the hearing prior to its issuance demonstrates that they intended it to require payment of all sums that became payable in July 1970, not just those stated for the first time in July. They note that Penn Central's Comptroller, Charles Hill, in explaining Penn Central's intention to pay "interline accounts to be presented after or scheduled to be presented after June 30," presented to the court an exhibit showing the amounts Penn Central planned to pay in July. Specifically included were drafts in the amount of $1 million for car repairs, which became subject to draft on July 15 under the AAR rules. Moreover, they note, Mr. Hill stated:

> The initial indication of actual disbursements begins with July 23 on revenue accounts, on July 13 on mileage accounts, and intermediate dates on car repairs.

The accounts that became subject to draft on July 15, would, under the AAR rules, represent May car repairs. Appellants also note that their counsel stated to the district court that if the order they proposed to the court in their motion of June 24, 1970, i.e., that Penn Central be required to pay *all* interline balances, were not granted that they would be satisfied with an order which "embraces those accounts and balances which Penn Central contemplates paying in July."

From this course of events, we conclude that the Interlines undoubtedly favored payment of interline accounts in full and that they proposed as a less drastic remedy that Penn Central be bound by its projections for July. Unfortunately, the step

we cannot take is to conclude that the district court accepted either of these positions. The district court, in inviting counsel to submit an order to it, stated that it was adopting the projections:

> The order which is being entered is not to be taken as either approval or disapproval of the projections set forth in these documents or of any of the projected expenditures.

The district court explained that it desired an order separating pre-petition interline charges from post-petition interline charges. It concluded that "charges stated from and after today would represent the post-petition interline balances" and specifically asked counsel to prepare an order providing for their payment.[13]

We think the court's oral statement pertaining to its order indicates that Order No. 9 did not contemplate the payment of all accounts that would become due for payment in July. The phrase "charges stated" is most reasonably interpreted as meaning charges first reported in the month of July. It strains the language unduly to interpret it to mean charges which have been previously reported but for which payment becomes due in July. The stark language in the actual order, ie., "stated or presented," could arguably be interpreted to encompass charges for which the drafts are presented in July, but we think the district court's statement to the parties as to the nature of the order he desired to enter precludes this interpretation.

We also believe that the district court's interpretation of its own order in the decision appealed from is entitled to great weight. We find no compelling basis to hold otherwise. We have

13. The court stated:

> From the evidence presented, it seems quite apparent that the post-petition interline charges, that is to say the charges stated from and after today would represent the post-petition inter-line balances, can be paid without unduly jeopardizing any of the other essential payments that the railroad must make.
>
> I therefore will enter an order and will invite counsel to submit the written order for entry which will make mandatory the payment of post-petition inter-line balances until further order of this Court.

already found that the parties' objections to the district court's entry of this order are without merit. They can petition the district court again if they believe that it should exercise its discretion to modify the order. We also note that the court in entering Order No. 9 provided explicitly that it would not prejudice the rights of the Interlines to claim a priority at a later time.

The order of the district court will be affirmed except as it operates to preclude the interline carriers from offsetting amounts they owe Penn Central against amounts Penn Central owes them for freight and passenger services. The Interlines shall be entitled to offset any amounts Penn Central owes them for freight and passenger services as of the date of this opinion, and Penn Central will be required to pay them immediately any remaining balances due for these accounts. The case will be remanded to the district court for the entry of an order consistent with this opinion.

ADAMS, *Circuit Judge*, concurring:

Though I concur in the result reached in this case, I am troubled by the heavy reliance by the majority upon the time-worn tenets of trust law in dealing with the issues presented here. Inasmuch as this appeal involves the functioning of the national transportation network, closer attention to pragmatic factors and to Congressional pronouncements would appear to be warranted.

Congress has long been concerned with the establishment and maintenance of a viable national rail system. In part, this concern is manifested in legislation tailored to encourage and facilitate "interline" rail transportation of freight and passengers.[1] To resort, as the majority does, primarily to "traditional common law trust principles" to resolve this case is to overlook the legislative policy embedded in these pertinent statutes. More-

1. *See, e.g.*, sections 1(4), 15(3), 15(4) and 15(6) of the Interstate Commerce Act, 49 U. S. C. §§ 1(4), 15(3), 15(4) and 15(6).

over, the majority's stance fails to address the practical problems confronting the railroad industry today. In this time of proliferating difficulty for the railroads, such an approach does little to advance the enterprise of "developing, coordinating and preserving a national transportation system."[2]

Section 1(4) of the Interstate Commerce Act[3] makes it the duty of each regulated rail carrier to participate in the interstate transportation of freight and passengers. In addition, it requires that the carriers "establish reasonable through routes with other such carriers, and just and reasonable rates, fare [and] charges . . . applicable thereto."[4] Carriers participating in through routes are directed to "provide reasonable facilities for operating such routes and . . . to make reasonable rules and regulations with respect to their operation . . . ." If connecting carriers fail to create voluntary through routes, section 15(3) of the Act[5] empowers the Interestate Commerce Commission, under certain conditions, to order their establishment.[6]

The policy underlying this statutory arrangement is not difficult to discern. "Interline," long-distance rail carriage over a through route obviates much of the need for duplicative, parallel rail lines. Additionally, through-route service precludes the inconvenience that would result if a shipper had to make separate arrangements with each interconnecting carrier for a long-distance haul. A vigorous and efficient interline rail network

2. The National Transportation Policy, 54 Stat. 899, 49 U. S. C. preceding § 1.

3. 49 U. S. C. § 1(4).

4. A "through route" is an arrangement between interconnecting railroads for the continuous carriage of goods or passengers from the originating point on the line of one carrier to a destination on the line of another. *See* St. Louis Southwestern Ry. Co. v. United States, 245 U. S. 136, 139 (1917).

5. 49 U. S. C. § 15(3).

6. *See generally* Thompson v. United States, 343 U. S. 549 (1952). Section 15(4) of the Act, 49 U. S. C. § 15(4), limits the power of the Commission to order a through route where to do so would force a railroad to "short haul" itself.

thus assures that, as the court below stated "[t]he nation's railroads function in many ways as a single system." The sections of the Interstate Commerce Act discussed above seek to foster and preserve this unitary rail scheme.

There is no statutory compulsion for interconnecting rail carriers to utilize any particular method of collecting fares and freight charges for a through-routed shipment. But, as a practical matter, only one such method is feasible. That is for a single carrier—either the originating or the destination carrier —to collect the entire fare, and then remit to the interline carriers their pro rata portions. This arrangement is apparently subscribed to by the entire industry, and is incorporated in the rules of the Association of American Railroads. A departure from this procedure—for example, insistence by each interline carrier upon immediate payment by the shipper—would likely undermine the entire system of interline rail transportation. At a minimum, it would greatly impede the smooth and efficient functioning of the through-route network.

At least one other court has concluded that, since practical considerations militate so strongly in favor of collection by a single carrier, that carrier should be deemed a "trustee" for the interline railroads.[7] Such a conclusion, when transposed to the scenario of a railroad reorganization case, requires that the interline carriers be granted a superior status vis-a-vis the trustee-railroad's other creditors. Conveniently, there are present in this case enough of the common indicia of a fiduciary relation-

7. Atlantic Coast Line R. Co. v. Pennsylvania R. Co., 12 F. Supp. 720, 722-23 (E. D. Pa. 1935). In a related case, the same court described a typical interline shipment:

> "[t]he service performed was a haul of citrous fruits from Florida to delivery points in the Northern States. A number of railroads, which we shall call five, participated in order in the carriage, making of it in one continuous haul. . . . The last link at the delivery end was the Pennsylvania Railroad. Because of a convenience so great as to be imperative, the Pennsylvania Company collected for the whole haul." Atlantic Coast Line R. Co. v. Pennsylvania R. Co., 12 F. Supp. 726 (E. D. Pa. 1935).

ship to support the majority's conclusion that here, too, the Penn Central holds the interlines' freight and passenger revenues in "trust." Consequently, and I believe correctly, the majority grants the interlines the preferred postion that "beneficiary" status merits under the relevant reorganization principles.

What the majority does not appear to consider, and what I suggest may be of critical importance, is the possibility that, in another case, the *absence* of any of the traditional indicators of a trust relationship would, under their view, require a contrary holding.[8] Exclusive reliance upon the precepts and terminology of trust law would seem, in such a case, to dictate that a court deny the interlines any priority over other creditors. Stripped of that priority, the interlines might well insist upon immediate payment from shippers for each segment of a long-distance haul. Such insistence, with the attendant dislocation of the through-route system, would be especially likely where, as here, the originating or destination carrier was on the verge of going into reorganization.

The disruption of interline transportation that might result from application of the majority's *ratio decidendi* to another case would seriously thwart the policy expressed in the Interstate Commerce Act. Moreover, it would tend to impede promotion of an "adequate, economical, and efficient" transportation system, thus hampering effectuation of our National Transportation Policy.[9] The majority does not address these considerations. Its approach, while leading to a salutary result in the case *sub judice*, overlooks these broader ramifications by focusing too narrowly upon the situation at hand.

Rather than merely invoke the hoary principles of trust law to settle this case, I would treat the problem of interline freight and passenger accounts as a *sui generis* matter. Having perceived Congress' interest in creating and maintaining a viable

8. Considering the turbulent, changing situation in the railroad industry, this does not seem a remote possibility.

9. *See* Note 2, *supra*, and accompanying text.

interline rail system, it would be appropriate to hold that, even in the *absence* of anything formally resembling a "trust," the interlines are entitled to a preferred position with respect to freight and passenger revenues owed them by a railroad in reorganization.

This is not to suggest that venerated legal doctrines can never provide guidance to a court confronted with novel questions of transportation law. But where Congress has, by statute and articulation of a national policy, prompted the judiciary to consider the effects of its decisions upon the nation's entire transportation system, there does not seem to be justification for exclusive reliance upon the narrow principles of private law.[10] The demands in treating a matter of national transportation policy are best met by a candid and informed weighing of competing interests, within the compass of the judicial process, rather than by use of dogmas or labels that may prove too inflexible to solve the non-Euclidean problems that are presented.

The majority also concludes that, unlike freight and passenger revenues, other interline monies—those relating to car repairs, overcharges, freight loss and damage, per diem car rentals, and switching charges—are *not* held in "trust." Since this holding would not appear to work any substantial disruption of the interline rail schema, I concur in this aspect of the result as well.

Judge Weis joins in this concurring opinion.

10. *Cf.* New Haven Inclusion Cases, 399 U. S. 392, 431 (1970).

IN THE UNITED STATES COURT OF APPEALS.
FOR THE THIRD CIRCUIT.

Nos. 72-1436, 72-1437, 72-1438.

In the Matter of:

PENN CENTRAL TRANSPORTATION COMPANY,
Debtor,

INDIANA HARBOR BELT RAILROAD COMPANY,
Appellant in No. 72-1436,

MEMBERS OF THE COMMITTEE OF INTERLINE RAILROADS: THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY, ET AL.,
Appellants in No. 72-1437,

LOUISVILLE AND NASHVILLE RAILROAD COMPANY,
Appellant in No. 72-1438.

Present: VAN DUSEN, ALDISERT, ADAMS, GIBBONS, ROSENN and WEIS, *Circuit Judges.*

ORDER.

It is Ordered that the slip opinion filed October 9, 1973, be amended as follows:

The word "immediately" in the last line of page 9 is deleted;

The word "immediate" in line 6, paragraph 2, page 20, is deleted;

The last two sentences in the final paragraph on page 23 are revised to read as follows:

The Interlines shall be entitled to offset any amounts Penn Central owes them for freight and passenger services as of the date of this opinion, and Penn Central will be obligated to pay any remaining balances due for these accounts. The case will be remanded to the district court for further proceedings consistent with this opinion.

By the Court,

MAX ROSENN,

Circuit Judge.

Dated: November 6, 1973.

UNITED STATES COURT OF APPEALS.
For the Third Circuit.

Nos. 72-1436, 72-1437, 72-1438.

In the Matter of:
PENN CENTRAL TRANSPORTATION COMPANY,
Debtor,
INDIANA HARBOR BELT RAILROAD COMPANY,
Appellant in No. 72-1436.

Members of the Committee of Interline Railroads:
The Atchison, Topeka and Santa Fe Railway Company
Illinois Northern Railway
Burlington Northern, Inc.
Oregon Trunk Railway
Chicago, Milwaukee, St. Paul and Pacific Railroad Company
Chicago & North Western Railway Co.
Chicago, Rock Island & Pacific Railroad Co.
Peoria Terminal Co.
Delaware & Hudson Railway Co.
Greenwich & Johnsonville Railway Co.
Grand Trunk Western Railroad Co.
Kansas City Southern Railroad
Louisiana & Arkansas Railway Co.
Missouri-Kansas-Texas Railroad Co.
Missouri Pacific Railroad Co.
Texas & Pacific Railway Co.
Missouri-Illinois Railroad Co.
Chicago & Eastern Illinois Railroad
Norfolk and Western Railway Co.
New Jersey, Indiana & Illinois Railroad
Norfolk, Franklin & Danville Railway

Seaboard Coast Line Railroad Co.
Columbia, Newberry & Laurens Railroad Co.
Southern Pacific Transportation Company
San Diego & Arizona Eastern Railway
Northwestern Pacific RR
Portland Traction Company
Sunset Railway Co.
Visalia Electric Railroad Co.
St. Louis Southwestern Railway Co.
Southern Railway System
St. Louis-San Francisco Railway Co.
Alabama, Tennessee & Northern Railroad Co.
Quanah, Acme & Pacific Railway Co.
Union Pacific Railroad Co.
The Western Pacific Railroad Co.
Sacramento Northern Railway,

Appellants in No. 72-1437,

Louisville and Nashville Railroad Company,

Appellant in No. 72-1438.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA.

(D. C. No. B-70-347 in Bankruptcy.)

Present: VAN DUSEN, ALDISERT, ADAMS, GIBBONS, ROSENN and WEIS, *Circuit Judges.*

AMENDED JUDGMENT ON REARGUMENT.

This cause came on to be heard on the record from the United States District Court for the Eastern District of Pennsylvania and was argued by counsel and later reargued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the order of the said District Court, filed March 16, 1972, be, and the same is hereby reversed, as it operates to preclude the interline carriers from offsetting amounts they owe Penn Central against amounts Penn Central owes them for freight and passenger services. The Interlines shall be entitled to offset any amounts Penn Central owes them for freight and passenger services as of the date of this judgment, and Penn Central will be required to pay them any remaining balances due for these accounts, all of the above in accordance with the opinion of this Court. In all other respects the said order of the said District Court be, and the same is hereby affirmed, and the cause remanded to the said District Court for further proceedings consistent with this opinion.

ATTEST:

THOMAS F. QUINN,

Clerk.

November 6, 1973.

UNITED STATES COURT OF APPEALS.
For the Third Circuit.

Nos. 72-1436, 72-1437, 72-1438.

In the Matter of:

PENN CENTRAL TRANSPORTATION COMPANY,
Debtor,

INDIANA HARBOR BELT RAILROAD COMPANY,
Appellant in No. 72-1436,

MEMBERS OF THE COMMITTEE OF INTERLINE RAILROADS: THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY, ET AL.,
Appellants in No. 72-1437,

LOUISVILLE AND NASHVILLE RAILROAD COMPANY,
Appellant in No. 72-1438.

ORDER SUR PETITIONS FOR REHEARING.

Present: VAN DUSEN, ALDISERT, ADAMS, GIBBONS, ROSENN, WEIS, *Circuit Judges.*

The petitions for rehearing filed by Penn Central Transportation Company, Appellee and Chicago and North Western Transportation Company, Appellant in the above entitled case having been submitted to the judges who participated in the decision of this court and to all the other available circuit

judges of the circuit in regular active service, and no judge who concurred in the decision having asked for rehearing, and a majority of the circuit judges of the circuit in regular active service not having voted for rehearing by the court in banc, the petitions for rehearing are denied.

By the Court,

MAX ROSENN,
Judge.

Dated: November 7, 1973.

STATUTORY PROVISIONS INVOLVED.

INTERSTATE COMMERCE ACT.

49 U. S. C. § 1(4).

(4) It shall be the duty of every common carrier subject to this part to provide and furnish transportation upon reasonable request therefor, and to establish reasonable through routes with other such carriers, and just and reasonable rates, fares, charges, and classifications applicable thereto; and it shall be the duty of common carriers by railroad subject to this part to establish reasonable through routes with common carriers by water subject to part III, and just and reasonable rates, fares, charges, and classifications applicable thereto. It shall be the duty of every such common carrier establishing through routes to provide reasonable facilities for operating such routes and to make reasonable rules and regulations with respect to their operation, and providing for reasonable compensation to those entitled thereto; and in case of joint rates, fares, or charges, to establish just, reasonable, and equitable divisions thereof, which shall not unduly prefer or prejudice any of such participating carriers.

49 U. S. C. § 1(10).

(10) The term "car service" in this part shall include the use, control, supply, movement, distribution, exchange, interchange, and return of locomotives, cars, and other vehicles used in the transportation of property, including special types of equipment, and the supply of trains, by any carrier by railroad subject to this part.

49 U. S. C. § 1(11).

(11) It shall be the duty of every carrier by railroad subject to this part to furnish safe and adequate car service and to establish, observe, and enforce just and reasonable rules, regulations, and practices with respect to car service; and every un-

just and unreasonable rule, regulation, and practice with respect to car service is prohibited and declared to be unlawful.

49 U. S. C. § 1(14)(a).

(14) (a) *The Commission may, after hearing, on a complaint or upon its own initiative without complaint, establish reasonable rules, regulations, and practices with respect to car service by common carriers by railroad subject to this part, including the compensation to be paid and other terms of any contract, agreement, or arrangement for the use of any locomotive, car, or other vehicle not owned by the carrier using it (and whether or not owned by another carrier), and the penalties or other sanctions for nonobservance of such rules, regulations, or practices.* In fixing such compensation to be paid for the use of any type of freight car, the Commission shall give consideration to the national level of ownership of such type of freight car and to other factors affecting the adequacy of the national freight car supply, and shall, on the basis of such consideration, determine whether compensation should be computed solely on the basis of elements of ownership expense involved in owning and maintaining such type of freight car, including a fair return on value, or whether such compensation should be increased by such incentive element or elements of compensation as in the Commission's judgment will provide just and reasonable compensation to freight car owners, contribute to sound car service practices (including efficient utilization and distribution of cars), and encourage the acquisition and maintenance of a car supply adequate to meet the needs of commerce and the national defense. The Commission shall not make any incentive element applicable to any type of freight car the supply of which the Commission finds to be adequate and may exempt from the compensation to be paid by any group of carriers such incentive element or elements if the Commission finds it to be in the national interest. (Emphasis supplied.)

49 U. S. C. § 15(8).

(8) In all cases where at the time of delivery of property to any railroad corporation being a common carrier, for transportation subject to the provisions of this part to any point of destination, between which and the point of such delivery for shipment two or more through routes and through rates shall have been established as in this part provided to which through routes and through rates such carrier is a party, the person, firm, or corporation making such shipment, subject to such reasonable exceptions and regulations as the Interstate Commerce Commission shall from time to time prescribe, shall have the right to designate in writing by which of such through routes such property shall be transported to destination, and it shall thereupon be the duty of the initial carrier to route said property and issue a through bill of lading therefor as so directed, and to transport said property over its own line or lines and deliver the same to a connecting line or lines according to such through route, and it shall be the duty of each of said connecting carriers to receive said property and transport it over the said line or lines and deliver the same to the next succeeding carrier or consignee according to the routing instructions in said bill of lading: *Provided, however,* That the shipper shall in all instances have the right to determine, where competing lines of railroad constitute portions of a through line or route, over which of said competing lines so constituting a portion of said through line or route his freight shall be transported.

BANKRUPTCY ACT.

11 U. S. C. § 205(j).

(j) *In addition to the provisions of section 29 of this title for the staying of pending suits against the debtor, the judge may enjoin or stay the commencement or continuation of suits against the debtor until after final decree; and may, upon notice and for cause shown, enjoin or stay the commencement or con-*

tinuance of any judicial proceeding to enforce any lien upon the estate until after final decree: Provided, That suits or claims for damages caused by the operation of trains, busses, or other means of transportation may be filed and prosecuted to judgment in any court of competent jurisdiction and any order staying the prosecution of any such cause of action or appeal shall be vacated. Proceedings under this section prior to its amendment by Act of August 27, 1935, or under this section as amended by such Act, shall not be grounds for the removal of any cause of action to the United States District Court which was not removable before March 3, 1933 and any order removing any cause of action or enjoining the prosecution of any such cause of action in any court is null and void and any cause of action heretofore removed from a State court, on account of this section prior to its amendment by Act of August 27, 1935, shall be remanded to the court from which it was removed. *The title of any owner, whether as trustee or otherwise, to rolling-stock equipment leased or conditionally sold to the debtor, and any right of such owner to take possession of such property in compliance with the provisions of any such lease or conditional sale contract, shall not be affected by the provisions of this section.* (Emphasis supplied.)

ORDER.

At a General Session of the Interstate Commerce Commission, held at its office in Washington, D. C., on the 15th day of July, A. D. 1930

No. 17801

Rules for car-hire settlement

It appearing, That by orders dated January 4 and June 7, 1926, the commission entered upon an investigation concerning the lawfulness of the rules for car-hire settlement between common carriers by railroad in the United States for the use and detention of freight cars while on the lines of carriers other than their owners, with a view to making such order or orders in the premises as may be warranted by the record;

It further appearing, That a full investigation of the matters and things involved has been had, and that the commission on January 7, 1930, made and filed a report containing its findings of fact and conclusions thereon, and on July 15, 1930, made and filed a supplemental report, which said report and supplemental report are hereby referred to and made a part hereof:

It is ordered, That respondents herein, as shown in the appendix hereto and made a part hereof, be, and they are hereby, notified and required to cease and desist, on or before October, 1, 1930, and thereafter to abstain, from applying rules for car-hire settlements which are in conflict with those prescribed for future application in the next succeeding paragraphs.

It is further ordered, That the said respondents herein be, and they are hereby, notified and required to establish, on or before October 1, 1930, and thereafter to maintain and observe, rules with respect to car-hire settlements which shall provide:

(1) That the same daily car rental shall be paid to common-carrier nonsubscribers as respondents contemporaneously pay to

subscribers to the per diem rules agreement of the American Railway Association, for the use of general-service freight cars.

(2) That similar reclaim allowances shall be made to non-subscribers as to subscribers of the per diem rules agreement, in connection with cars handled in terminal switching service, as the latter term is defined by the switching reclaim rules of the American Railway Association.

(3) That short-line railroads which are less than 100 miles in length, and which return railroad-owned equipment to the road from which received, shall not be required to report per diem accruals to numerous car owners throughout the country, but shall be attached to their connecting carriers for purpose of car-hire settlement.

(4) That common-carrier railroads which interchange freight cars with more than one subscriber railroad, and which deliver to one or more subscribing carriers, freight cars which are received from another such carrier, and railroads 100 miles or more in length, regardless of the number of railroads with which they connect, shall make car-hire settlements direct with car owners in accordance with the per diem rules.

(5) That common-carrier railroads outside switching districts, other than those referred to in paragraph 4 hereof, shall pay per diem to connecting carriers on railroad-owned freight cars after deducting an average of two days free time per loaded freight car interchanged, settlements to be made at the end of each calendar month, except that no car hire need be paid on cars received for return loading with coal from coal mines which are customarily dependent upon connecting carriers for car supply.

It is further ordered, That this order shall continue in effect until the further order of the commission.

And it is further ordered, That all unexpired orders, or parts of unexpired orders, heretofore entered in the proceedings consolidated with and made a part of this proceeding, be, and they are hereby, vacated and set aside in so far as in conflict with our order herein.

APPENDIX.

[The Order and Appendix thereto comprised 19 pages. The Appendix beginning on page 2 and ending on page 19 contained a list (about 1000 names) of all the railroad respondents to the proceeding, which names have been eliminated for the convenience of the Court. The Appendix closed on page 19, following the last named railroad, with:]

By the commission.

GEORGE B. MCGINTY,
Secretary.

[SEAL]

(XIX)

U. S. Government Printing Office: 1930

Service Date
May 28, 1970

ORDER.

At a General Session of the INTERSTATE COMMERCE COMMISSION, held at its office in Washington, D. C., on the 28th day of May, A. D. 1970.

No. 31358*

CHICAGO, BURLINGTON & QUINCY R. R. CO., ET AL.

vs.

NEW YORK, SUSQUEHANNA & WESTERN R. R. CO., ET AL.

Upon consideration of the record in the above-entitled proceedings; the Commission's report and order on further hearing in *Chicago, B. & Q. R. Co.*, v. *New York, S. & W. R. Co.*, 332 I. C. C. 176; the judgment by the Supreme Court of the United States entered January 12, 1970, denying the petitions for rehearing filed by the appellants, Union Pacific Railroad Co., et al., in *Arizona Corporation Commission, et al.* v. *United States, et al.* and *Union Pacific Railroad Co., et al.* v. *United States, et al.*, Nos. 480 and 497, October Term 1969; the *per curiam* orders entered November 10, 1969, by said Court in Nos. 343, 480, and 497, October Term 1969, summarily affirming judgments entered by the United States District Courts for the Districts of Massachusetts and Nebraska in *Boston and Maine Railroad* v. *United States*, 297 F. Supp. 318 (1969), and *Union Pacific Railroad Company* v. *United States*, 300 F.

* Embracing No. 33145, *Railroad Freight Car Per Diem Charges* and No. 34405, *Southern Railway Company et al.* v. *The Pennsylvania Railroad Company, et al.*

Supp. 318 (1969); our order entered January 29, 1970, in the above-entitled proceedings; our order entered herein on February 26, 1970, postponing the effective date from March 1, 1970, to June 1, 1970; and of the letter-request of the Chairman of the House Committee on Interstate and Foreign Commerce, dated May 25, 1970, for the postponement of the date set by our order of February 26, 1970, for institution of the prescribed charges in the future, in order to allow the committee and the Congress sufficient time in which to reach a determination on pertinent legislation now set to be heard in the near future; and good cause appearing therefor:

It is ordered, That the date by which the rail carriers affected by the order of the Commission, dated February 26, 1970, are required to comply with said order insofar as it institutes prescribed charges for the future, be, and it is hereby, postponed from June 1, 1970, to September 1, 1970, and no further postponement is contemplated.

By the Commission.

H. NEIL GARSON
Secretary

(SEAL)

SUPREME COURT OF THE UNITED STATES

MAR 6 1974

MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

October Term, 1973.

No. 73-1201.

CHICAGO AND NORTH WESTERN TRANSPORTATION COMPANY, GRAND TRUNK WESTERN RAILROAD COMPANY and ST. LOUIS-SAN FRANCISCO RAILWAY COMPANY,

Petitioners,

v.

GEORGE P. BAKER, RICHARD C. BOND, and JERVIS LANGDON, JR., TRUSTEES OF THE PROPERTY OF PENN CENTRAL TRANSPORTATION COMPANY, DEBTOR,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

BRIEF FOR RESPONDENTS IN OPPOSITION

PAUL R. DUKE,
JOHN B. ROSSI,
1138 Six Penn Center,
Philadelphia, Pa. 19104

RICHARD R. BONGARTZ,
61 Howland Road,
Westport Harbor, Mass. 02790

Attorneys for Respondents.

International Printing Co., 711 So. 50th St., Phila., Pa. 19143 — Tel. (215) 727-8711

INDEX

	Page
Opinions Below	1
Question Presented	2
Statutes Involved	2
Statement of the Case	3
Reasons for Denying the Writ	7
Conclusion	11
Appendix—Statutory Provisions Involved	B1

TABLE OF CASES CITED

	Page
Ahnapee & W. Ry. Co. v. Akron & B.B.R. Co., 302 I.C.C. 265 (1957)	8
Baltimore & O.R. Co. v. New York, N.H. & H.R. Co., 196 F. Supp. 724 (S.D.N.Y. 1961)	8
Boston & Maine Corp. v. Chicago, Burlington & Quincy R., 258 F. Supp. 930 (S.D.N.Y. 1966), aff'd. 381 F.2d 365 (2d Cir. 1967)	6
Chicago, R.I. & P. Ry. Co. v. U.S., 284 U.S. 80 (1931)	8
In re New York, New Haven and Hartford Railroad Co., 278 F. Supp. 592 (D. Conn. 1967), aff'd. 405 F.2d 50 (2d Cir. 1968)	11
In re Penn Central Transportation Co., 453 F.2d 520 (3d Cir. 1971), cert. den. 408 U.S. 923 (1972)	9
In re Penn Central Transportation Co., 477 F.2d 841 (3d Cir. 1973), aff'd. sub nom. U.S. Steel Corp. v. Trustees of Penn Central Trans. Co., — U.S. — (42 L.W. 3213), and cert. den. sub nom. In re Penn Central Trans. Co., — U.S. — (42 L.W. 3213)	9
Rules for Car Hire Settlement, 160 I.C.C. 369, 165 I.C.C. 495 (1930)	7, 8

MISCELLANEOUS

	Page
Bankruptcy Act (11 U.S.C. 205(b)):	
Section 77	2, 3, 10
Section 77(b), (c)(4) and (c)(7)	2, 11
Interstate Commerce Act (49 U.S.C. § 5b(2)):	
Section 5a(2) and (6)	2, 8

IN THE

Supreme Court of the United States

OCTOBER TERM, 1973.

No. 73-1201.

CHICAGO AND NORTH WESTERN TRANSPORTATION COMPANY, GRAND TRUNK WESTERN RAILROAD COMPANY AND ST. LOUIS-SAN FRANCISCO RAILWAY COMPANY,

Petitioners,

v.

GEORGE P. BAKER, RICHARD C. BOND, AND JERVIS LANGDON, JR., TRUSTEES OF THE PROPERTY OF PENN CENTRAL TRANSPORTATION COMPANY, DEBTOR,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR RESPONDENTS IN OPPOSITION

OPINIONS BELOW

The opinion of the United States District Court for the Eastern District of Pennsylvania is reported at 340 F. Supp. 857 (E.D. Pa. 1972) and is printed in the Appendix

(A1) to the Petition. The opinion of the Court of Appeals for the Third Circuit, filed October 9, 1973, as amended by its order filed November 6, 1973, is reported at 486 F.2d 519 (3d Cir. 1973). The opinion and amending order are printed in the Appendix (A16, A43) to the Petition.

QUESTION PRESENTED

Whether the United States Court of Appeals for the Third Circuit was correct in affirming the decision of the United States District Court for the Eastern District of Pennsylvania that the per diem net balances owing to petitioners at the time that the Debtor railroad went into reorganization under Section 77 of the Bankruptcy Act did not constitute a trust and were not entitled to payment or setoff against amounts owing to respondents on other interline accounts, and that whether such balances are entitled to an equitable lien and priority over other creditors should await classification of claims in the proof of claims program.

STATUTES INVOLVED

Section 77(b), (c)(4) and (c)(7) of the Bankruptcy Act (11 U.S.C. 205(b), (c)(4) and (c)(7)), Section 5a(2) and (6) of the Interstate Commerce Act (49 U.S.C. § 5b(2) and (6)) are set forth in pertinent part in the Appendix hereto (B1 to B3).

STATEMENT OF THE CASE

The respondents are the Trustees of the property of Penn Central Transportation Company (Penn Central), Debtor in reorganization under Section 77 of the Bankruptcy Act in the United States District Court for the Eastern District of Pennsylvania, No. 70-347. Among the unpaid debts of Penn Central when it filed its petition for reorganization on June 21, 1970, were amounts owing on account of per diem for rental of freight cars of other railroads which came due on June 10, 1970, for use of the cars of such railroads, including petitioners, in April, 1970, and prior months.

In addition to these per diem accounts, Penn Central also owed other railroads for other interline accounts such as freight and passenger charges, switching, car repairs, loss and damage and freight overcharges. In turn, such other railroads owed Penn Central balances on interline accounts.

Under Order No. 1 in its reorganization proceeding, Penn Central was authorized, in its discretion, to pay all current expenses incurred in operating, maintaining and preserving its railroad, including all interline accounts and balances owing by the Debtor. Not content with this authorization regarding payment of post-bankruptcy accounts, Burlington Northern, Inc., a railroad creditor, sought and obtained Order No. 9, an amendment to Order No. 1 (Jt. App. 32a) [1] directing the Debtor to pay such balances as they became due. Order No. 9 was without prejudice to creditor railroads to claim a priority with respect to pre-bankruptcy interline accounts and balances.

---

1. The reference "Jt. App. —a" is to the Joint Appendix filed in the Court of Appeals. The reference "A—" is to the Appendix to the Petition. The reference "Pet. —" is to the Petition itself.

Other railroads, including petitioners, then proceeded to offset what Penn Central owed them on account of pre-bankruptcy interline accounts against what they owed Penn Central for such accounts. Because of such action, the Penn Central Trustees were deprived of revenue approximating $4.3 million and they petitioned their Reorganization Court to enjoin such setoffs, which were contrary to Order No. 1 in the Penn Central reorganization proceeding (Jt. App. 34a).[2] The railroads against which such action was brought, including petitioners, claimed that the pre-bankruptcy interline balances owed to them by Penn Central constituted a trust, that they were entitled to payment, or in the alternative, that equitable liens should be impressed on account of such balances, and that they were entitled to set them off against amounts that they owed Penn Central, pre-bankruptcy, on account of interline balances. The Reorganization Court rejected these contentions and enjoined the setoffs, without prejudice to assertion of claims for priority of interline accounts over other creditors at a later date in the proof of claims program (A10-12).

On appeal to the United States Court of Appeals for the Third Circuit, that Court held that the interline freight and passenger balances owed to other railroads by the Debtor constituted a trust and ordered payment of such balances. This holding is the subject of a petition to this Court by the Trustees of Penn Central for a writ of certiorari, October Term, 1973, No. 73-914. In other respects,

---

2. In Order No. 1, entered June 21, 1970, it was provided (paragraph 10):

> "All persons, firms and corporations . . . holding for the account of the Debtor deposit balances or credits be and each of them hereby are restrained and enjoined from selling, converting or otherwise disposing of such collateral, deposit balances or other credits, or any part thereof, or from off-setting the same, or any thereof, against any obligation of the Debtor, until further order of this Court."

the Court of Appeals affirmed the decision of the Reorganization Court, holding that there was no trust relationship for interline accounts other than freight and passenger, and, that in the absence of a trust relationship on other accounts, whether to permit a setoff is in the discretion of the district court, which had not abused its discretion. Through the Court of Appeals' affirmance of the Reorganization Court with respect to other interline accounts, the status of such other interline accounts, including per diem, was deferred to the classification of claims under the proof of claims program.

Although the Code of Car Hire Rules and Disbursements Mandatory Rules provide that net balances for per diem are subject to draft immediately upon the report of per diem balances, which is no later than the tenth day of the second month following that in which the per diem accrued (Jt. App. 76a-77a), petitioners' drafts for net per diem balances owing by the Debtor on the June, 1970, reporting date were not presented for payment until after the inception of the Debtor's reorganization proceeding on June 21, 1970 (Pet. p. 8).

Under the Accounting Rules of the Association of American Railroads, which apply to interline accounts, each account is settled on its own, either on a gross or net basis, and interline balances covering different accounts, *e.g.*, freight and per diem, could not be netted (Jt. App. 78a-79a). Petitioners were attempting to accomplish such netting of different accounts by setting off other accounts owed to Penn Central against the per diem owed to them by Penn Central.

Under procedures pursuant to the Mandatory Arbitration Rules of the Association of American Railroads it was held in Interline Freight Arbitration Case No. 20141, *Boston and Maine Corporation v. Chicago and North-*

western Railway Company, that C&NW violated Freight Mandatory Rule 149 when it refused to honor B&M's drafts for settlement of interline freight balances because of an unrelated dispute between the two roads concerning car service balances (Jt. App. 79a). A similar arbitration award was upheld in *Boston & Maine Corp. v. Chicago, Burlington & Quincy R.*, 258 F. Supp. 930 (S.D.N.Y. 1966), *aff'd.* 381 F.2d 365 (2d Cir. 1967).

REASONS FOR DENYING THE WRIT

The petition should be denied because it attempts to obtain a decision from this Court on matters which both the Reorganization Court and the Circuit Court of Appeals have left open for future consideration in the program for classification of claims in the Debtor's reorganization proceeding. In this respect, the instant petition differs entirely from that of the Penn Central Trustees filed at Docket No. 73-914. Denial of the Penn Central Trustees' petition would completely foreclose any further relief with respect to the question of the status of freight and passenger interline balances. Here, the question of the status of per diem claims is left open for determination at a later stage in the proceedings.

Petitioners argue at length that their claims for prebankruptcy net interline per diem balances are those of involuntary creditors superior to the claims of voluntary creditors, but it does not follow that the Court of Appeals, in affirming the decision of the Reorganization Court, was in error in holding that petitioners were not entitled to payment or setoff, or to a declaration of an equitable lien for such claims at this time.

Petitioners' arguments with respect to the nature of their interline claims were fully considered by both Courts and it is of no consequence to their decisions that petitioners did not then refer to *Rules for Car Hire Settlement*, 160 I.C.C. 369, 165 I.C.C. 495 (1930), regarding their claim of involuntary creditor status. The only significance of the lower Courts' not noting this decision is the tacit concession by petitioners (Pet. p. 11) that their present argument with respect to this decision was not presented to either Court, and is now cited for the first time in this Court. Nor, in the light of the thrust of the decision of

the Court of Appeals, can it be said that it is in conflict with this Court's decision in *Chicago, R.I. & P. Ry. Co. v. U.S.*, 284 U.S. 80 (1931), in which the Court upheld the car hire settlement rules approved by the Commission.

In making its statement that "there is no compulsion, statutory or otherwise as to the manner by which the services shall be paid," to which petitioners take exception, the Court of Appeals was considering whether set-offs should be allowed or payments required with respect to the car repair, overcharge, loss and damage, per diem, and switching accounts. Nor is it certain that as to the periods covered by these claims there was any compulsion even with respect to per diem. The 1930 Commission decision relied on by petitioners antedated by 18 years the enactment by Congress of Section 5(a) of the Interstate Commerce Act which requires that, with respect to any agreement among carriers relating, *inter alia*, to the compensation paid for the use of equipment, the right of independent action of any carrier be preserved free and unrestrained. Interstate Commerce Act, §§5a(2), 5a(6), 49 U.S.C. §§5b(2), 5b(6). Until the Interstate Commerce Commission prescription of rates became effective in September, 1970 (after the period here in question), certain railroads did exercise that right, despite the alleged compulsion of the Rules for Car Hire Settlement. See *Ahnapee & W. Ry. Co. v. Akron & B.B.R. Co.*, 302 I.C.C. 265 (1957); *Baltimore & O.R. Co. v. New York, N.H. & H.R. Co.*, 196 F. Supp. 724, 731-735 (S.D.N.Y. 1961).

In any event, the Court's holding that the amounts owing on these accounts could not be set off was based on the conclusion that they were not held in trust which was premised on the recognition that no money is collected as to these accounts by Penn Central for other railroads and

did not depend on whether arrangements for payment or credit were voluntary (A32-33).

After its holding that a trust did not exist for these debtor-creditor accounts, the Court of Appeals reaffirmed the Reorganization Court's authority to preclude setoffs.

> ". . . The threat to the reorganization that we noted in the *Bank Cases* is present in the assertion of these setoffs. Penn Central's choses in action for the various interline charges are entitled to the same status as the freight charges in the *Shipper Cases* and the deposits in the *Bank* Cases. The district court concluded that to permit setoffs could discriminate against many other suppliers of services and equipment and would be unfair because of the unresolved issue of the relative priorities of claims. It also concluded that Penn Central's cash position would be unduly injured by allowing setoffs.
>
> "In the absence of a trust relationship, whether to permit a setoff is in the discretion of the district court. See *Susquehanna Chemical Corp. v. Producers Bank & Trust Co.*, 174 F.2d 783, 786-87 (3d Cir. 1949). We find no abuse of discretion in the circumstances of this case." (A35)[3]

As already noted, petitioners have not been precluded from asserting their claims for per diem balances in the Debtor's reorganization proceeding. As stated by the Reorganization Court in prohibiting setoffs (A10):

3. The "Bank Cases" referred to in the quoted material are *In re Penn Central Transportation Co.*, 453 F.2d 520 (3d Cir. 1971), *cert. den.* 408 U.S. 923 (1972). The "Shipper Cases" are *In re Penn Central Transportation Co.*, 477 F.2d 841 (3d Cir. 1973), *aff'd.* sub nom. *U.S. Steel Corp. v. Trustees of Penn Central Trans. Co.*, — U.S. — (42 L.W. 3213), and *cert. den.* sub nom. *In re Penn Central Trans. Co.*, — U.S. — (42 L.W. 3213).

"... The claims of the interline railroads arose out of transactions which were a vital part of the Debtor's day-to-day business. Such claims would probably fall within the so-called 'six-months' rule' which has been held applicable in § 77 proceedings, and would likely be entitled to a high priority. *E.g.*, 5 *Collier on Bankruptcy*, par. 77.21 nn. 27-29 (1970).

"But, just as in the 'shippers' case,' several factors persuade me that set-offs should be prohibited at this time. First, to permit set-offs could discriminate against the many other suppliers of services and equipment to the Debtor. At the hearing on July 1, it was estimated that pre-petition claims by these suppliers would aggregate over $200 million. In view of the substantial uncertainty that the interline railroads will be able to establish a distinction between their claims and the claims of the Debtor's trade creditors, it would not be appropriate to permit the interline railroads to resolve the question favorably to themselves through the self-help remedy of set-off prior to determination of the question in the proof of claims program."

Likewise, with respect to the interline railroads' claim for an equitable lien, the Reorganization Court held that a decision should await the classification of the interline railroads' claims in the proof of claims program, noting that other creditors had not had the opportunity to express themselves (A11).

In these circumstances, the petition does not present a matter which warrants a determination by this Court. The procedures for the establishment and status of petitioners' per diem claims in the Debtor's reorganization proceeding are provided in Section 77 of the Bankruptcy Act and the decisions of the courts below are without prejudice to their

resort to such procedures. In other railroad reorganization proceedings, the status of pre-bankruptcy interline per diem claims has been determined in classification of claims in a proof of claims program under Section 77(b), (c)(4) and (c)(7), and such determination should be made with respect to petitioners' per diem claims. See *In re New York, New Haven and Hartford Railroad Co.*, 278 F. Supp. 592 (D. Conn. 1967), *aff'd.* 405 F.2d 50 (2d Cir. 1968).

CONCLUSION

This petition for a Writ of Certiorari should be denied.

Respectfully submitted,

PAUL R. DUKE,
JOHN B. ROSSI,
1138 Six Penn Center,
Philadelphia, Pa. 19104

RICHARD R. BONGARTZ,
61 Howland Road,
Westport Harbor, Mass. 02790
Attorneys for Respondents.

Appendix.

STATUTORY PROVISIONS INVOLVED.

Interstate Commerce Act.

49 U.S.C. § 5b(2).

(2) Any carrier party to an agreement between or among two or more carriers relating to rates, fares, classifications, divisions, allowances, or charges (including charges between carriers and compensation paid or received for the use of facilities and equipment), or rules and regulations pertaining thereto, or procedures for the joint consideration, initiation or establishment thereof, may, under such rules and regulations as the Commission may prescribe, apply to the Commission for approval of the agreement, and the Commission shall by order approve any such agreement (if approval thereof is not prohibited by paragraph (4), (5), or (6) of this section) if it finds that, by reason of furtherance of the national transportation policy declared in this Act, the relief provided in paragraph (9) of this section should apply with respect to the making and carrying out of such agreement; otherwise the application shall be denied. The approval of the Commission shall be granted only upon such terms and conditions as the Commission may prescribe as necessary to enable it to grant its approval in accordance with the standard above set forth in this paragraph.

49 U.S.C. § 5b(6).

(6) The Commission shall not approve under this section any agreement which establishes a procedure for

the determination of any matter through joint consideration unless it finds that under the agreement there is accorded to each party the free and unrestrained right to take independent action either before or after any determination arrived at through such procedure.

Bankruptcy Act.

11 U.S.C. § 205(b).

(b) . . . The term "claims" includes debts, whether liquidated or unliquidated, securities (other than stock and option warrants to subscribe to stock), liens, or other interests of whatever character. For all purposes of this section unsecured claims, which would have been entitled to priority if a receiver in equity of the property of the debtor had been appointed by a Federal court on the day of the approval of the petition, shall be entitled to such priority and the holders of such claims shall be treated as a separate class or classes of creditors . . .

11 U.S.C. § 205(c)(4).

(c)(4) The judge shall require the officers of the debtor or the trustee or trustees, at such time or times as the judge may direct, and in lieu of the schedules required by section 7 of this Act, to file with the court such schedules and submit such other information as may be necessary to disclose the conduct of the debtor's affairs and the fairness of any proposed plan; and shall direct the officers of the debtor, or the trustee or trustees, within such time as the judge shall set, to prepare and file with the court a list of all known bondholders and creditors of the debtor, and the amounts and character of their debts, claims, and securities, and the last known post-office address or place of business of each bondholder and creditor, and a list of all known

stockholders of the debtor, with the last known post-office address or place of business of each, which lists the judge may require to be brought down to date at any time. The contents of such lists shall not constitute admissions by the debtor or the trustees in a proceeding under this section or otherwise.

11 U.S.C. § 205(c)(7).

(c)(7) The judge shall promptly determine and fix a reasonable time within which the claims of creditors may be filed or evidenced and after which no claim not so filed or evidenced may participate except on order for cause shown, the manner in which such claims may be filed or evidenced and allowed, and for the purposes of the plan and its acceptance, after notice and hearing, the division of creditors and stockholders into classes according to the nature of their respective claims and interests. Such division shall not provide for separate classification unless there be substantial differences in priorities, claims, or interests. The trustee or trustees under any mortgage, deed of trust, or indenture outstanding against the property may, within the time prescribed, file a verified claim in behalf of all bonds or securities outstanding under such mortgage, deed of trust, or indenture, in which event it shall be unnecessary for the holders of such bonds or securities to file claims in their own behalf, but nothing herein shall constitute such trustee or trustees the representative or representatives of such holders for the purpose of accepting or rejecting any plan of reorganization.

LIBRARY
SUPREME COURT, U. S.

FILED
MAR 19 1974
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1973

No. 73-1201

CHICAGO AND NORTH WESTERN TRANSPORTATION COMPANY, GRAND TRUNK WESTERN RAILROAD COMPANY AND ST. LOUIS-SAN FRANCISCO RAILWAY COMPANY,

Petitioners,

vs.

GEORGE P. BAKER, RICHARD C. BOND, AND JERVIS LANGDON, JR., TRUSTEES OF THE PROPERTY OF PENN CENTRAL TRANSPORTATION COMPANY, DEBTOR,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

REPLY BRIEF OF PETITIONERS

RICHARD M. FREEMAN,
ZEV STEIGER,
400 West Madison Street,
Chicago, Illinois 60606,
Attorneys for Petitioners.

Gunthorp-Warren Printing Company, Chicago • 346-1717

IN THE

Supreme Court of the United States

OCTOBER TERM, 1973.

No. 73-1201

CHICAGO AND NORTH WESTERN TRANSPORTATION COMPANY, GRAND TRUNK WESTERN RAILROAD COMPANY AND ST. LOUIS-SAN FRANCISCO RAILWAY COMPANY,

Petitioners,

vs.

GEORGE P. BAKER, RICHARD C. BOND, AND JERVIS LANGDON, JR., TRUSTEES OF THE PROPERTY OF PENN CENTRAL TRANSPORTATION COMPANY, DEBTOR,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

REPLY BRIEF OF PETITIONERS

Petitioners submit this brief in reply to the arguments first raised in the brief for Respondents in opposition to the petition, as authorized by Rule 24.4.

I

THE SIGNIFICANCE OF WHETHER PETITIONERS DID NOT VOLUNTARILY EXTEND CREDIT FOR PER DIEM

Respondents have failed to fully appreciate the significance (to the decisions below and to the petition) of the question whether Petitioners voluntarily extended credit for per diem, for

they suggest (Resp. pp. 8-9) that Petitioners' right to payment, setoff or other relief before the Reorganization Court depends on whether the amounts owing for per diem are held in trust, and not upon whether Petitioners voluntarily extended credit for such amounts.

The opinion of the Reorganization Court is premised on the holding that credit was voluntarily extended; therefore, the Court reasons, "equitable principles" (A9) did not require payment or justify permitting setoff or other relief for the present. It is clear from the text and headings of its opinion that the Reorganization Court first set out (under the heading "A. The Right of the Interline Railroads to Payment of Their Claims." (A7)) to determine if "equitable principles" (A7, 9) entitled the railroads to payment of their claims, and, following its holding that the railroads voluntarily extended credit to the Debtor (Penn Central)—on the ground that "self-help" measures were available to put Penn Central on a cash basis for all interline accounts (A9)—the Court concluded that the railroads are not presently entitled to payment of their claims. Then the Reorganization Court proceeded (under the heading "B. Control of the Exercise of the Right of Set-Off." (A9)) to determine not only whether it *could* enjoin setoffs but also whether it *should* enjoin the railroads from setting off. The Court enjoined setoff of per diem and other interline accounts primarily on the ground that *there was "substantial uncertainty that the interline railroads will be able to establish a distinction between their claims and the claims of the Debtor's trade creditors,* [and] it would not be appropriate to permit the interline railroads to resolve the question favorably to themselves through the self-help remedy of set-off prior to determination of the question in the proof of claims program." (Emphasis added) (A10). Neither the Reorganization Court nor the Court of Appeals (which affirmed as to all interline accounts except freight and passenger) appreciated the distinction between per diem and other interline accounts on the matter of "self-help."

The essence of Petitioners' position is that they had no lawful means of "self-help" by which to protect themselves against non-payment of their per diem balances; that they did not voluntarily extend credit to Penn Central; and that, for these and other reasons set forth in the petition (particularly the operation of Section 1(14)(a) of the Interstate Commerce Act), their per diem claims are clearly distinguishable, as a matter of law, from the claims of trade and other voluntary creditors. Accordingly, per diem claims are, as a matter of law, entitled to immediate payment. However, even if immediate payment is not required as a matter of law, but is held to be within the discretion of the Reorganization Court, the distinctive equities vested in per diem claims should entitle Petitioners, as unique involuntary creditors, to an order requiring payment or permitting setoff or other appropriate relief (including declaration of constructive trust) for such claims. As pointed out in the petition, since the opinion of the Reorganization Court was premised on the holding that credit was voluntarily extended for per diem, it is possible, and indeed likely, that the Reorganization Court would have ordered payment of per diem claims or permitted setoff or other appropriate relief, if that Court had found that self-help was not available for per diem and that there was no voluntary extension of credit.*

---

* Although the right of setoff does not automatically apply in reorganization proceedings, but may be enjoined "to save a sick business" (*Susquehanna Chemical Corp.* v. *Producers Bank & Trust Co.*, 174 F. 2d 783, 787 (3d Cir. 1949)), it does not follow that setoff will automatically be enjoined. Whether a setoff may properly be enjoined "depends upon the equities of the situation" (*Id.*, at 787). Thus, where setoffs would "frustrate the reorganization process" they have been enjoined. *Penn Central Transportation Company* v. *National City Bank of Cleveland, et al.*, 315 F. Supp. 1281, 1283 (E. D. Pa. 1970), *aff'd*, 453 F. 2d 520 (3d Cir. 1971), *cert. den.*, 408 U. S. 923 (1972). But, here, given the equities vested in per diem claims and the clear distinction between voluntary and involuntary creditors (and between per diem creditors and other involuntary creditors, if any) the Reorganization Court would not be justified in enjoining setoff for per diem on "discrimination" grounds or on the ground that such setoffs would frustrate reorganization. Any setoff means a reduction in the debtor's receivables

II

NEWLY CITED AUTHORITIES

As Respondents correctly point out (Resp. p. 7), Petitioners have acknowledged that they did not cite to either the Reorganization Court or the Court of Appeals the decisions and order of the Commission in *Rules for Car Hire Settlement*, 160 I. C. C. 369, 165 I. C. C. 495 (1930) or the decision of this Court in *Chicago, R. I. & P. Ry. Co.* v. *U. S.*, 284 U. S. 80 (1931). Of course, Petitioners regret that these obviously pertinent and controlling authorities for their position on per diem claims were discovered only shortly before the due date of the petition, well after the Court of Appeals denied petitions for rehearing. However, the argument that per diem claims are involuntary and do not reflect an ordinary debtor-creditor relationship, and that Petitioners are entitled to payment, setoff and other relief, was presented in the pleadings (Pet. pp. 8-9; Resp. p. 4) and was otherwise before the Reorganization Court and the Court of Appeals. Further there was fully presented to the Court of Appeals, on petition for rehearing, the argument (including criticism of

---

(but not in its current cash position), yet this is justified in appropriate cases on grounds of equity. Penn Central would be thus affected by setoff of per diem, but it cannot be said, nor did the Reorganization Court find, that such setoff would frustrate reorganization. The per diem amounts involved (while substantial for Petitioners) are minute (for Penn Central) compared to the staggering cash and non-cash requirements for Penn Central's successful reorganization, and this was known to be so on June 21, 1970. Although "changed circumstances" are not before this Court on this petition (*e.g.*, the *Regional Rail Reorganization Act of 1973*, Public Law 93-236, 93d Congress, approved Jan. 2, 1974, 87 Stat. 985), the Court may take judicial notice of the fact that permitting setoff or other relief, even for all railroad per diem claims (not only Petitioners'), would have no material adverse effect on Penn Central's reorganization or on its financial condition.

For other forms of possible relief for per diem claims see *In re New York, New Haven & Hartford Railroad Co.*, 330 F. Supp. 131 (1971), *rev'd on jurisdictional grounds*, 457 F. 2d 683 (2d Cir. 1972), in which Judge Anderson, on equitable grounds includ-

Southern Ry. Co. v. *Flournoy*, 301 F. 2d 847 (4th Cir. 1962) (Pet. p. 12) that the manner of *car hire settlement* is compelled by operation of the Interstate Commerce Act and practical necessity, so there is no lawful "self-help" for per diem and no voluntary extension of credit. Moreover, it is evident that Petitioners are relying on more than the newly cited authorities, for as stated at page 8 of the petition:

> ". . . there was no voluntary extension of credit to Penn Central. *Even without the Commission order,* Petitioners had no lawful means by which to protect themselves against non-payment of their per diem balances. They could not withhold their cars, and since any demand by them for cash settlement or security would be disregarded by Penn Central with impunity, there was nothing more they could have done (or could do now) to protect themselves against non-payment." (Emphasis added, footnotes deleted.)

It is worth noting that Respondents' only response to this is a paragraph on the "right of independent action" (Resp. p. 8) containing a conspicuously weak near-denial, namely, that it was not certain that there was any compulsion with respect to per diem. What is more telling, however, is Respondents' failure to comment on the error of the courts below on the issue of "self-help", as applied to per diem, and their failure to cite even one action which could have been taken by Petitioners to assure payment of per diem balances.

III

THE "RIGHT OF INDEPENDENT ACTION"

In citing the "right of independent action" (preserved under Sections 5(a)(2) and 5(a)(6) of the Interstate Commerce Act) to suggest that there may not have been any element of

---

ing unjust enrichment (p. 144), imposed an equitable lien on former New Haven properties transferred to Penn Central and declared a constructive trust on other such properties and on income therefrom; and *In re Penn Central Transportation Company*, 337 F. Supp. 779, 790 (1972), in which Judge Fullam imposed a "tentative lien" on the former New Haven properties, in favor of the New Haven Trustee.

compulsion (Resp. p. 8), Respondents entirely miss the point that there was no "independent action" which Petitioners could have taken to assure payment of their per diem balances. Moreover, Respondents obscure and misapprehend the clear distinction between cases involving disputes over the level of per diem (*i.e.*, what is the reasonable compensation required by Section 1(14)(a) of the Interstate Commerce Act?) and this case, involving no dispute over the level of per diem or the per diem amounts owed to Petitioners, but rather the issue whether (in the words of the Court of Appeals) there is "compulsion, statutory or otherwise, as to the manner by which [per diem] shall be paid." (A32) The railroads referred to by Respondents as having exercised the right of independent action (Resp. p. 8) did so only because they objected to the *level* of per diem determined pursuant to agreed AAR procedures, and not because they objected to, or could have disregarded, the practices and rules for car hire *settlement* prescribed in the AAR Code of Per Diem Rules and the order of the Commission in *Rules for Car Hire Settlement, supra.* In fact, even as these railroads litigated before the Commission and the courts the per diem level issue, they continued (or attempted) to report and settle car hire in accordance with the terms of the Commission order and the settlement rules of the AAR Code of Per Diem Rules. Such litigation included the arbitration cases cited by Respondents (Resp. pp. 5-6), which concerned attempts by car-owning railroads to set off *disputed* per diem amounts claimed to be due from car-using railroads, against undisputed freight balances owed to such car-using railroads. In the subject proceeding, however, there is no issue over the amount of Petitioners' per diem claims or Penn Central's obligation to pay; the issue is whether, because of the unique characteristics of per diem claims, the Reorganization Court must (or should) order payment now or permit setoff or other appropriate relief for such claims.

IV

OTHER RAILROAD REORGANIZATION PROCEEDINGS

It may be a fact, as Respondents assert (Resp. p. 11) that in other reorganization proceedings "the status of pre-bankruptcy interline per diem claims has been determined in classification of claims in a proof of claims program . . ." It is also a fact, which Respondents fail to state, that the arguments for immediate payment of per diem claims, setoff, declaration of constructive trust or other relief, asserted by Petitioners in the petition, were never raised or articulated in those other proceedings, but were first raised and argued before the courts in this proceeding. It is also worth noting that Respondents do not mention, let alone discuss, the operation of Section 1(14)(a) of the Interstate Commerce Act, upon which Petitioners' reasons for granting the petition are, in part, based; nor do Respondents comment on the unlimited financial risk a car-owning railroad is forced to assume if the decisions below are allowed to stand. Although it cannot refuse to permit use of its cars by other roads, before or during their reorganization, and cannot protect itself against their non-payments of per diem balances, it must suffer what may be a serious drain on working capital through a forced wait of many years (consider Penn Central's likely timetable!) before the status of its per diem claims is determined and payment, if any, is received. And compounding this inequity is the fact that, throughout the period of non-payment of per diem, the car-using railroad earns freight revenues through use of the car-owning railroad's cars.

CONCLUSION

For the reasons stated herein and in the petition, certiorari should be granted.

Respectfully submitted,

RICHARD M. FREEMAN,
ZEV STEIGER,
400 West Madison Street,
Chicago, Illinois 60606,
Attorneys for Petitioners, Chicago and North Western Transportation Company, Grand Trunk Western Railroad Company and St. Louis-San Francisco Railway Company.